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

FORM 20–F

☐ REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the fiscal year ended December 31, 2012

OR

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

OR

☐ SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report…….

For the transition period from _____ to _____

Commission file number 000–26495

COMMTOUCH SOFTWARE LTD.

(Exact name of Registrant as specified in its charter and
translation of Registrant's name into English)

Israel
(Jurisdiction of incorporation or organization)

1 Sapir Road
5th Floor, Beit Ampa
P.O. Box 4014
Herzliya 46140, Israel
011–972–9–863–6888
(Address of principal executive offices)

Brian Briggs, CFO, 7927 Jones Branch Drive, Suite 2250, Tysons Corner, VA 22102, Fax: 703-760-3321.
(Name, Telephone, Email and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Ordinary Shares, par value NIS 0.15 per share	**NASDAQ Capital Market**

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report (December 31, 2012).

Ordinary Shares, par value NIS 0.15	25,826,234

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐No ☒

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ☐No ☒

Note: Checking the above box will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐No

Indicate by check mark 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. Check one:

Large accelerated filer ☐	Accelerated filer ☐	Non-accelerated filer ☒

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing.

U.S. GAAP ☒	International Financial Reporting Standards as issued by the International Accounting Standards Board ☐	Other ☐

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. Item 17 ☐ Item 18 ☐

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐No ☒

PART I

Item 1. Identity of Directors, Senior Management and Advisers.

Not applicable.

Item 2. Offer Statistics and Expected Timetable.

Not applicable

Item 3. Key Information.

Unless otherwise indicated, all references in this document to "Commtouch," "the Company," "we," "us" or "our" are to Commtouch Software Ltd. or its wholly-owned subsidiaries (directly or indirectly), Commtouch Inc., Commtouch Iceland hf, and eleven Gesellschaft zur Entwicklung und Vermarktung von Netzwerktechnologien mbH, or eleven, as relating to consolidated financial information contained herein.

The selected consolidated statements of income data for the years ended December 31, 2010, 2011 and 2012 and the selected consolidated balance sheet data as of December 31, 2011 and 2012 have been derived from the Consolidated Financial Statements of Commtouch included elsewhere in this Annual Report on Form 20-F, or this Annual Report. The selected consolidated statements of operations data for the years ended December 31, 2008 and 2009 and the selected consolidated balance sheet data as of December 31, 2008, 2009 and 2010 have been derived from the Consolidated Financial Statements of Commtouch not included elsewhere in this Annual Report. Our historical results are not necessarily indicative of results to be expected for any future period. The data set forth below should be read in conjunction with "Item 5. Operating and Financial Review and Prospects" and the Consolidated Financial Statements and the Notes thereto included elsewhere herein:

	Year Ended December 31,				
	2008	2009	2010	2011	2012
	(USD and share amounts in thousands, except per share data)				
Selected Data:					
Revenues	$ 14,092	$ 15,189	$ 18,161	$ 23,016	$ 23,910
Operating income	$ 1,931	$ 2,696	$ 3,360	$ 3,308	$ 780
Net income attributable to ordinary and equivalently participating shareholders	$ 2,270	$ 5,160	$ 4,403	$ 4,598	$ 1,485
Basic net earnings per share	$ 0.09	$ 0.21	$ 0.19	$ 0.19	$ 0.06
Diluted net earnings per share	$ 0.08	$ 0.20	$ 0.18	$ 0.19	$ 0.06
Weighted average number of shares used in computing basic net earnings per share	25,619	24,532	23,575	23,620	24,610
Weighted average number of shares used in computing diluted net earnings per share	26,929	25,292	24,874	24,654	25,140
Total Assets	$ 20,709	$ 25,190	$ 31,982	$ 39,534	$ 59,133

FORWARD LOOKING STATEMENTS

Except for the historical information contained in this Annual Report, the statements contained in this Annual Report are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, as amended, and other federal securities laws with respect to our business, financial condition and results of operations. Such forward-looking statements reflect our current view with respect to future events and financial results.

We urge you to consider that statements which use the terms "anticipate," "believe," "expect," "plan," "intend," "estimate" and similar expressions are intended to identify forward-looking statements. We remind readers that forward-looking statements are merely predictions and therefore inherently subject to uncertainties and other factors and involve known and unknown risks that could cause the actual results, performance, levels of activity, or our achievements, or industry results, to be materially different from any future results,

performance, levels of activity, or our achievements, or industry results, expressed or implied by such forward-looking statements. Such forward-looking statements appear in Item 4 – "Information on the Company" and Item 5 – "Operating and Financial Review and Prospects," as well as elsewhere in this Annual Report. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Except as required by applicable law, including the securities laws of the United States, we undertake no obligation to update or revise any forward-looking statements to reflect new information, future events or circumstances, or otherwise after the date hereof. We have attempted to identify significant uncertainties and other factors affecting forward-looking statements in the Risk Factors section that appears below.

RISK FACTORS

You should carefully consider the following risk factors before you decide to buy our Ordinary Shares. You should also consider the other information in this Annual Report. If any of the following risks actually occur, our business, financial condition, operating results or cash flows could be materially adversely affected. This could cause the trading price of our Ordinary Shares to decline, and you could lose part or all of your investment. The risks described below are not the only ones facing us. Additional risks not presently known to us, or that we currently deem immaterial, may also impair our business operations.

Business Risks

If we are unable to effectively integrate the businesses of eleven and Frisk into our global organization, our operating results will suffer.

During 2012, we acquired both the antivirus business of the Icelandic company Frisk Software International, or Frisk, and the German Internet security company eleven and, in connection therewith, we literally doubled the size of our organization in terms of personnel (though at the beginning of 2013 we performed an approximately 12% synergistic reduction of headcount to better streamline the organization). For a somewhat small organization such as Commtouch, the acquisition of two companies within less than six months, in two very different parts of the world, is an extremely complex and challenging venture. While we believe that in the future, these acquisitions will be very fruitful for the growth of the Company, in the short term, these acquisitions are stretching our internal resources, both financial and manpower.

Our ability to attain our sales, marketing and development goals will depend in great measure on our ability to create one cohesive organization that is focused on the goals set by a unified management. Should the efforts at integrating these new businesses into Commtouch not continue in a smooth or successful fashion, our business will suffer and shareholder value will decline. Furthermore, any such failure could impact our efforts at acquiring an additional company or technologies during 2013 and beyond.

If the market does not continue to respond favorably to our traditional Internet security solutions, including our anti-spam, Zero-Hour antivirus, Mail Reputation, Command Antivirus and Uniform Resource Locator or URL filtering solutions, or our new cloud-based solutions or our future solutions do not gain acceptance, we will fail to generate sufficient revenues.

Our success depends on the continued acceptance and use of our traditional Internet security solutions by current and new businesses, Original Equipment Manufacturers, or OEMs, and service provider customers, plus the interest of such customers in our newest offerings. We have been selling our inbound anti-spam products for over nine years, our Zero-Hour™ virus outbreak detection product for approximately eight years, our GlobalView™ Mail Reputation perimeter defense solution for approximately seven years, our URL filtering solutions for over three years, our outbound spam solution for approximately three years and the Command Antivirus solution for over two years. Also, we recently released three new cloud-based Internet security solutions – a) email Security as a Service, or email "SecaaS", b) Commtouch Mobile Security Services for Android and c) Commtouch Email Security On-Premise for Service Providers.

As the markets for messaging, antivirus and Web security products continue to mature and consolidate, we are seeing increasing competitive pressures and demands for even higher quality products at lower prices. This increasing demand comes at a time when Internet security threats are more varied and intensive, challenging even the top end solutions to keep their performance at an industry acceptable high level of accuracy. If our solutions do not continue to evolve to meet market demand, or newer products on the market prove more effective, our business could fail. Also, if growth in the markets for these solutions begins to slow, our business will suffer dramatically.

Recurring unfavorable national and global economic conditions could have a material adverse effect on our business, operating results and financial condition.

The crisis in the financial and credit markets that began in 2008 in the United States, and that led to a global economic slowdown, seems to have become more acute in certain countries of Europe. If the economies of countries in which our customers and potential customers are located continue to be weak or weaken further, our customers may reduce or postpone their spending significantly. This could result in reductions in sales of our services and longer sales cycles, slower adoption of new technologies and increased price competition. In addition, weakness in the end-user market could negatively affect the cash flow of our OEM and service provider partners, distributors and resellers who could, in turn, delay paying their obligations to us. This would increase our credit risk exposure and cause delays in our recognition of revenues on future sales to these customers. Specific economic trends, such as declines in the demand for PCs, servers, and other computing devices, or weakness in corporate information technology spending, could have a more direct impact on our business. Any of these events would likely harm our business, operating results and financial condition.

If economic conditions in key markets do not improve or continue to improve, or revert to a recessionary state, our business, operating results and financial condition may be adversely impacted in a material way.

Tighter governmental enforcement of regulations could decrease the distribution of unsolicited bulk (spam) email and malicious software and decrease demand for our solutions, or increase our cost of doing business.

The Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 (CAN-SPAM Act) established a framework of U.S. administrative, civil, and criminal tools to combat spam. The law establishes both civil and criminal prohibitions to assist in deterring the most offensive forms of spam, including unmarked sexually-oriented messages and emails containing fraudulent headers. Under the law, senders of email are required to honor a request by a consumer not to receive any further unsolicited messages. While past high profile prosecutions of direct marketers seemingly have not had much of a deterrent effect on marketers of unsolicited email, it is not known whether or not future enforcement actions will prove effective.

In addition, various state legislatures have enacted laws aimed at regulating the distribution of unsolicited email. While we are not clear as to the reasons, two years ago we began to see a gradual decline in the amount of spam traffic on the Internet, and in the past year spam activity remained consistent at this lower level.

These and similar legal measures, both in the United States and worldwide, may have the effect of reducing the amount of unsolicited email and malicious software that is distributed and hence diminish the need for our Internet security solutions. Any such developments would have an adverse impact on our revenues.

We depend upon OEM partners, service providers and resellers.

We expect to continue to be dependent upon OEM partners and service providers for a significant portion of our revenues, which will be derived from sales of our messaging, antivirus and Web security solutions. We also expect resellers to become more important in the distribution of our newer cloud-based Internet security solutions. Our operating results and financial condition may be materially adversely affected if:

- Anticipated orders or payments from these customers fail to materialize;
- Some of the key customers cease the promotion of our business or begin to promote additional solutions in a layered approach to email defense, anti-malware and URL filtering management; or
- Some of our key customers' businesses fail as a result of a deepening global economic crisis.

Our quarterly operating results may fluctuate, which could adversely affect the value of your investment.

A number of factors, many of which are enumerated in this "Risk Factors" section, are likely to cause fluctuations in our operating results or cause our share price to decline. These factors include:

- Our ability to successfully market both our traditional messaging, antivirus and Web security solutions and our newer cloud-based Internet security solutions in new markets, both domestic and international;
- Our ability to successfully develop and market new, modified or upgraded solutions, as may be needed;
- The continued acceptance of our solutions by our current customer base;
- Our ability to expand our workforce with qualified personnel, as may be needed;
- Unanticipated bugs or other problems affecting the delivery of our solutions to customers;
- The success of our customers' sales efforts to their customer base;
- The solvency of our customers and their ability to allocate sufficient resources towards the marketing of our solutions;
- Our customers' ability to effectively integrate our solutions into their product offerings;
- The substantial decrease in information technology spending;
- The pricing of our solutions;
- Our ability to timely collect fees owed by our customers;
- A renewed global slowdown;
- Sudden, dramatic fluctuations in exchange rates of currencies covering the fees we collect from our foreign customers versus the currencies utilized in our business (namely, the New Israeli Shekel, or NIS, the U.S. Dollar and Euro);
- Our ability to add cost-effective space and equipment to our current detection centers, or Detection Centers, in a timely and effective manner to match the rate of growth in our business, plus our ability to build new, cost-effective detection centers as worldwide demand for our products may require; and
- The effectiveness of our end user support, whether provided by our customers or directly by Commtouch.

Our products and services have changed many times since we commenced operations in 1991. For example, in September 2010, we acquired the Command Antivirus unit of Authentium, and during 2012 (as noted above) we acquired both the Frisk antivirus business and all of the business of eleven, and we have integrated and continue to integrate these new business into our existing business. These and future changes in our product offerings may require that we adjust our business processes and workforce, which can cause disruption to our business and fluctuations in our results from operations.

We have many established competitors who are offering a multitude of solutions to the problems of spam/virus distribution and Web-related security threats.

The market for Internet security products remains intensely competitive and is subject to rapid changes in technology. We expect both product and pricing competitive pressures to increase in the future. Some of our competitors have longer operating histories, greater brand recognition, larger technical staffs and/or greater financial, technical and marketing resources, and other advantages compared to us. This competition could have a negative impact on our business and financial results. Additional details are provided in Item 4. "Information on the Company."

Our ability to continue to increase our revenues will depend on our ability to successfully execute our sales and business development plan.

The complexity of the underlying technological base of messaging, antivirus and Web security solutions, and the current landscape of the markets, require highly trained sales and business development personnel to educate prospective resellers, OEM and service provider partners and customers regarding the use and benefits of our solutions. During 2012, with the acquisitions of Frisk's antivirus business and eleven, as well as natural turnover in sales personnel, our business development/sales department underwent a higher rate of change than in prior years. It may take time for our current and future employees to convey to potential, as well as current, OEM/service provider partners and resellers how to most effectively market and utilize our solutions. As a result, our sales and business development

personnel may not be able to compete successfully against larger, more heavily financed and experienced sales and business development departments of our competitors.

The loss of our key employees would adversely affect our ability to manage our business, therefore causing our operating results to suffer and the value of your investment to decline.

Our success depends on the skills, experience and performance of our senior management and other key personnel. The loss of the services of any of our senior management or other key personnel could materially and adversely affect our business. The loss of our software developers or senior operations personnel may also adversely affect the continued development and support of both our current messaging, antivirus and Web security solutions and future solutions presently included in our roadmap for development, thereby causing our operating results to suffer and the value of your investment to decline.

We do not have employment agreements inclusive of set periods of employment with any of our key personnel. We cannot prevent them from leaving at any time. We do not maintain key-person life insurance policies, listing us as a beneficiary, on any of our employees.

Our business and operating results could suffer if we do not successfully address potential risks inherent in doing business overseas.

As of December 31, 2012, we had sales offices in Israel the United States, Germany and Iceland. We also are marketing our messaging, antivirus and Web security solutions in international markets by utilizing appropriate distribution channels. However, we may not be able to compete effectively in international markets due to various risks inherent in conducting business internationally, such as:

- Differing technology standards;
- Inability of distribution channels to successfully market our solutions;
- Export restrictions;
- Difficulties in collecting accounts receivable and longer collection periods;
- Unexpected changes in regulatory requirements;
- Political and economic instability;
- Potentially adverse tax consequences; and
- Limited enforcement mechanisms for protecting intellectual property rights.

Any of these factors could adversely affect the Company’s prospective international sales and, consequently, business and operating results.

Our Web security and antivirus solutions may be adversely affected if we are not able to receive sufficient components from third party suppliers.

Our Web security solution relies in part on certain components supplied by third parties pursuant to contractual relationships. If these third parties breach their agreements with us, we may have difficulty in securing alternative sources for these components in a timely manner and thus our Web security solution may not perform at the level we expect. If this were to occur, the effectiveness of this solution would drop, it would become less attractive to customers/potential customers and anticipated revenues could decline.

Technology Risks

We may not have the resources or skills required to adapt to the changing technological requirements and shifting preferences of our customers and their users.

The messaging, antivirus and Web security industries are characterized by difficult technological challenges, sophisticated distributors of Internet security threats, multiple-variant viruses, unique phishing scams and constantly evolving malevolent software distribution practices and targets that could render our solutions and proprietary technology ineffective. Our success depends, in part, on our ability to continually enhance our existing messaging, antivirus and Web security solutions and to develop new solutions, functions and technology that address the potential needs of prospective and current customers and their users. The development of proprietary technology and necessary

enhancements entails significant technical and business risks and requires substantial expenditures and lead-time. We may not be able to keep pace with the latest technological developments. We may not be able to use new technologies effectively or adapt to OEM, service provider, customer or end user requirements or emerging industry standards. Also, we must be able to act more quickly than our competition, and may not be able to do so.

Our solutions may be adversely affected by defects or denial of service attacks, which could cause our OEM and service provider partners, customers or end users to stop using our solutions.

Our messaging, antivirus and Web security solutions are based in part upon new and complex software and highly advanced computer systems. Complex software and computer systems can contain defects, particularly when first introduced or when new versions are released, and are possible targets for denial of service attacks instigated by "hackers". Although we conduct extensive testing and implement Internet security processes, we may not discover defects to or vulnerabilities in our software or systems that affect our new or current solutions or enhancements until after they are delivered. Although we have not experienced any material defects or vulnerabilities to date in our messaging, antivirus and Web security offerings, it is possible that, despite testing by us, defects or vulnerabilities may exist in the solutions we provide. These defects or vulnerabilities could cause or lead to interruptions for customers of our solutions, resulting in damage to our reputation, legal risks, loss of revenue, delays in market acceptance and diversion of our development resources, any of which could cause our business to suffer.

Our messaging, antivirus and Web security solutions may be adversely affected if we are not able to receive a sufficient sampling of Internet traffic or our Detection Centers were to become unavailable.

Our messaging, antivirus and Web security solutions are dependent, in part, on the ability of our Detection Centers to analyze, in an automated fashion, live feeds of Internet and Web related traffic received through our services to customers and other contractual arrangements. If we were to suffer an unanticipated, substantial decrease in such traffic or our multiple Detection Centers become unavailable for any significant period, the effectiveness of our technologies would drop, our product offerings would become less attractive to customers/potential customers and revenues could decline.

Our Antivirus offerings remain relatively new for us, and we still may not fully appreciate the needs of customers and risks inherent in these new markets.

Our acquisition of the antivirus business from Authentium in September 2010, followed up by our acquisition of Frisk's antivirus business in October 2012, represented our first efforts at expansion into the antivirus market. While we hired the core team of ex-Authentium and ex-Frisk employees and contractors who possess the expertise to manage the antivirus business, nevertheless we cannot be totally certain that we have anticipated all possible issues that might arise with our "cloud computing" technology infrastructure and our relatively new antivirus offerings. Should unanticipated issues arise, sales of our antivirus solutions likely will slow and our business will suffer.

For example, because of the complexity of the antivirus products, we understand that in the past, errors were found in versions of these products that were not detected before first introduced, or appeared in new versions or enhancements, and we may find such errors in the future. Failures, errors or defects in our antivirus solutions could result in security breaches or compliance violations for our customers, disruption or damage to their networks or other negative consequences and could result in negative publicity, damage to our reputation, declining sales, increased expenses and customer relation issues. Such failures could also result in product liability damage claims against us by our customers, even though our agreements with our customers typically contain provisions designed to limit our exposure to potential product liability claims.

The antivirus products have in the past, and may at times in the future, falsely detect viruses or computer threats that do not actually exist. These false alarms, while typical in the security industry, would likely impair the perceived reliability of our products and may therefore adversely impact market acceptance of our antivirus products.

Our new cloud-based offerings have not been on the market for very long, so we may not see the customer traction in these offerings that we anticipate.

In November 2012, we acquired eleven, in part to accelerate our push into the cloud-based Internet security sector. The solutions we are promoting and will promote to this market will enable Internet security vendors and service providers to offer fully cloud-based, Internet security solutions to their customers, without the need for the integration of a software development kit, or SDK, into their product offerings. Among other things, this cloud-based approach is intended to speed up the process of moving our solutions to market, and ease the integration burden for our customers.

While eleven had successfully penetrated the German market with its solutions, it did not have a significant international presence. With Commtouch's international infrastructure – both in terms of business development and operations – we feel that we should be better positioned to succeed in markets outside of Germany. However, we do not have a record of success with our new offerings, including our a) email SecaaS, b) Commtouch Mobile Security Services for Android and c) Commtouch Email Security On-Premise for Service Providers. We will also be releasing new cloud-based solutions during the course of 2013 that will utilize new technologies that we acquired. Because of the newness of the technologies involved and the resulting learning curve required of all employees in the sale and support of the new offerings, we cannot be certain that we will convince potential customers of the benefits of these new offerings and sell them at the rate we anticipate. If we fall short of our expectations, and especially given the significant resources invested by us in bringing these new offerings to market, our financial results will suffer and the value of shareholder investments will decline.

Investment Risks

If we will be in need of additional capital, we may not be able to secure additional funds on acceptable terms, or at all, and the Company's business could suffer.

We have invested heavily in technology development, and in the past two and a half years we have closed three acquisitions. We expect to continue to spend financial and other resources on developing, acquiring and introducing new offerings and maintaining our corporate organizations and strategic relationships. We also expect to continue to invest resources in research and development projects to further enhance our current solutions.

Given the heavy outlays in capital expended during 2012 in both M&A activities and internal development, the Company's cash balance has dropped significantly and thus the Company is more thinly capitalized in 2013 than it was during the majority of 2012. As a result, at about the time of the filing of this Annual Report, a credit line had been secured from an Israeli bank, and we were in the process of closing on another credit line with a second Israeli bank. Together, both credit lines total a sum of up to $5,000,000. These credit lines are being put in place in order to ensure sufficient cash is available to fund the strategic growth investments of the Company.

In relation to these credit lines, the Company has agreed to grant security interests generally over all Company assets, and to refrain from encumbering its assets in favor of any other third parties. The Company has already drawn on one of the credit lines in the amount of $1.5 million.

While we believe that the credit lines will be sufficient to bridge any cash flow issues in the near term, if we will be in need of additional capital and are unable to secure it on acceptable terms or at all and, concurrently, customer collections will be slower than normal, the Company's business will suffer.

Our business could be materially adversely affected as a result of the risks associated with acquisitions and investments. In particular, we may not succeed in making additional acquisitions or be effective in integrating such acquisitions.

As part of our growth strategy, we have made a number of acquisitions over the past few years, including a total of three acquisitions during the years 2010 through 2012, and expect to continue to make acquisitions. We frequently evaluate the tactical or strategic opportunity available related to complementary businesses, products or technologies. The process of integrating an acquired company's business into our operations and/or of investing in new technologies, may result in unforeseen operating difficulties and large expenditures and may absorb significant management attention that would otherwise be available for the ongoing development of our business, and which may result in the loss of key customers and/or personnel and expose us to unanticipated liabilities.

Other risks commonly encountered with acquisitions include the effect of the acquisition on our financial and strategic position, the inability to successfully integrate or commercialize acquired technologies and achieve expected synergies or economies of scale on a timely basis and the potential impairment of acquired assets. Further, we may not be able to retain the key employees that may be necessary to operate the business we acquire, and, we may not be able to timely attract new skilled employees and management to replace them. From time to time, we may also need to acquire complementary technologies, whether to execute our strategies or in order to comply with customer needs. There are no assurances that we will be able to acquire or successfully integrate an acquired company, business or technology, or successfully leverage such complementary technology in the market.

Moreover, there can be no assurance that the anticipated benefits of any acquisition or investment will be realized. Future acquisitions or investments could result in potentially dilutive issuances of equity securities, the incurrence of debt and contingent liabilities, amortization expenses related to intangible assets and impairment of goodwill, any of which could have a material adverse effect on our operating results and financial condition. In addition, we may knowingly enter into an acquisition that will have a dilutive impact on our earnings per share.

There can be no assurance that we will be successful in making additional acquisitions or effective in integrating such acquisitions into our existing business. We may also compete with others to acquire companies, and such competition may result in decreased availability of, or increased prices for, suitable acquisition candidates. In addition, for possible commercial and economic considerations, we may not be able to consummate acquisitions that we have identified as crucial to the implementation of our strategy. We may not be able to obtain the necessary regulatory approvals, including those of competition authorities and foreign investment authorities, in countries where we seek to consummate acquisitions. For those and other reasons, we may ultimately fail to consummate an acquisition, even if we announce that we plan to acquire a company.

Due to changes in the industry and market conditions, we could also be required to realign our resources and consider restructuring or other action, which could result in an impairment of goodwill.

Our directors, executive officers and principal shareholders will be able to exert significant influence over matters requiring shareholder approval and could delay or prevent a change of control.

Our directors and affiliates of our directors, our executive officers and our shareholders who currently individually beneficially own over five percent of the voting power in the Company (together known as “affiliated entities”), beneficially own, in the aggregate, approximately 29.3% of our outstanding Ordinary Shares as of March 1, 2013. Included in the calculation of voting power are options exercisable by the affiliated entities within 60 days thereof (with some having an exercise price greater than the market price of our shares as of March 1. 2013). If they vote together (especially if they were to exercise all vested options into shares entitled to voting rights in the Company), these shareholders will be able to exercise significant influence over many matters requiring shareholder approval, including the election of directors and approval of significant corporate transactions. In this regard, we know of no shareholders or voting agreement between major shareholders or between such shareholders and directors or officers.

This concentration of ownership could also delay or prevent a change in control of Commtouch. In addition, conflicts of interest may arise as a consequence of the significant shareholders control relationship with us, including:

- Conflicts between significant shareholders, and our other shareholders whose interests may differ with respect to, among other things, our strategic direction or significant corporate transactions;
- Conflicts related to corporate opportunities that could be pursued by us, on the one hand, or by these shareholders, on the other hand; or
- Conflicts related to existing or new contractual relationships between us, on the one hand, and these shareholders, on the other hand.

Our Ordinary Shares are traded on more than one market and this may result in price variations.

Our Ordinary Shares are traded primarily on the NASDAQ Capital Market and also on the Tel Aviv Stock Exchange. Trading in our Ordinary Shares on these markets is made in different currencies (U.S. dollars on the NASDAQ Capital Market, and NIS, on the Tel Aviv Stock Exchange), and at different times (resulting from different time zones, different trading days and different public holidays in the United States and Israel). Consequently, the trading prices of our Ordinary Shares on these two markets often differ. Any decrease in the trading price of our Ordinary Shares on one of these markets could cause a decrease in the trading price of our Ordinary Shares on the other market.

Intellectual Property Risks

If we fail to adequately protect our intellectual property rights or face a claim of intellectual property infringement by a third party, we could lose our intellectual property rights or be liable for significant damages.

We regard our patented and patent pending technology, copyrights, service marks, trademarks, trade secrets and similar intellectual property as critical to our success, and rely on patent, trademark and copyright law, trade secret protection and confidentiality or license agreements with our employees and customers to protect our proprietary rights. See Item 4. Information on the Company, *Intellectual Property* for information pertaining to our patent activities. We may seek to patent certain additional software or other technology in the future. Any such patent applications might not result in patents issued within the scope of the claims we seek, or at all.

Despite our precautions, unauthorized third parties may copy certain portions of our technology, reverse engineer or obtain and use information that we regard as proprietary or otherwise infringe or misappropriate our patent or our patent pending technology, trade secrets, copyrights, trademarks and similar proprietary rights. In addition, the laws of some foreign countries do not protect proprietary rights to the same extent as do the laws of the United States. Thus, our means of protecting our proprietary rights in the United States or abroad, as well as our financial resources, may not be adequate, and competitors may independently develop similar technology.

We cannot be certain that our Internet security solutions do not infringe issued patents in certain parts of the world. Therefore, other parties, whether in the United States or elsewhere, may assert infringement claims against us. We may also be subject to legal proceedings and claims from time to time in the ordinary course of our business, including claims of alleged infringement of copyrights, trademarks and other intellectual property rights of third parties by ourselves and our customers. Our customer agreements typically include indemnity provisions, so we may be obligated to defend against third party intellectual property rights infringement claims on behalf of our customers. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources. We may not have the proper resources in order to adequately defend against such claims. During 2011, one such indemnification demand was made by a customer, and we continue to cooperate with that customer in seeking to defeat the underlying patent infringement claims. While we believe that adequate non-infringement and/or invalidity arguments exist, we are uncertain if the case will proceed to judgment. During early 2013, we learned that our customer is negotiating a settlement of the matter, and we have been asked to contribute a portion towards the settlement. It is too early in the negotiations process to anticipate the outcome of the settlement negotiations and our possible contribution towards any final settlement.

Risks Relating to Operations in Israel

We have important facilities and resources located in Israel, which has historically experienced military and political unrest.

Commtouch Software Ltd. is incorporated under the laws of the State of Israel. Our principal research and development facilities are located in Israel. Although the majority of our past sales were made to customers outside Israel, we are nonetheless directly influenced by the political, economic and military conditions affecting Israel. Any major hostilities involving Israel, or the interruption or curtailment of trade between Israel and its present trading partners, could significantly harm our business, operating results and financial condition.

Since the State of Israel was established in 1948, a number of armed conflicts have occurred between Israel and its Arab neighbors. Recent years have witnessed extensive hostilities from time to time along Israel's northern and southern borders, which resulted in missiles being fired from Lebanon and the Gaza Strip into Israel. Ongoing and revived hostilities or other Israeli political or economic factors could harm our operations and cause our revenues to decrease.

Recent uprisings in various countries in the Middle East and North Africa, known generally as the "Arab Spring", are affecting the political stability of those countries. This instability in the region may lead to deterioration of the political and trade relationships that exist between the State of Israel and certain of these and other countries. In addition, this instability may affect the global economy and marketplace, including as a result of increases in oil and gas prices. In addition, Israel and some companies doing business with Israel have been the subject of an economic boycott by Arab countries and their close allies since Israel's establishment.

The regional instability and restrictive laws and policies described above may have an adverse impact on our operating results, financial condition and expansion of our business.

Our results of operations may be negatively affected by the obligation of key personnel to perform military service.

Certain of our officers and employees are currently obligated to perform annual reserve duty in the Israel Defense Forces and are subject to being called for active military duty at any time in the event of a national emergency, such as in connection with the hostilities along Israel's border with the Gaza Strip in December 2008 and January 2009. Although Commtouch has operated effectively under these requirements since its inception, we cannot predict the effect of these obligations on Commtouch in the future. Our operations could be disrupted by the absence for a significant period of one or more of our officers or key employees due to military service. Any disruption in our operations would harm our business.

Because a substantial portion of our revenues historically have been generated in U.S. dollars and the Euro, and a significant portion of our expenses have been incurred in NIS, our results of operations may be adversely affected by currency fluctuations.

We have generated a substantial portion of our revenues in U.S. dollars and Euro, and incurred a portion of our expenses, principally salaries and related personnel expenses in Israel, in NIS. We anticipate that a significant portion of our expenses will continue to be denominated in NIS. As a result, we are exposed to risk to the extent that the value of the U.S. dollar decreases against the NIS and the Euro. In that event, the U.S. dollar cost of our operations will increase and our U.S. dollar-measured results of operations will be adversely affected, as occurred during a portion of 2011, when the NIS and the Euro appreciated against the U.S. dollar, which resulted in a significant increase in the U.S. dollar cost of our operational expenses and revenues. We cannot predict the trend for future years. Our operations also could be adversely affected if we are unable to guard against currency fluctuations in the future. To date, we have not engaged in any significant hedging transactions. In the future, we may enter into currency hedging transactions to decrease the risk of financial exposure from fluctuations in the exchange rate of the dollar against the NIS. Foreign currency fluctuations, and our attempts to mitigate the risks caused by such fluctuations, could have a material and adverse effect on our results of operations and financial condition.

The government programs and benefits which we previously received require us to meet several conditions and may be terminated or reduced in the future.

Prior to 1998, we received grants from the Government of Israel, through the Office of the Chief Scientist of the Israeli Ministry of Industry, Trade & Labor, or OCS, for the financing of a significant portion of our research and development expenditures in Israel. These grants totaled $0.6 million. Subsequently, in 2001, we received $0.6 million and in 2002 we received $0.2 million. We did not submit an application for funding during the period 2004 – 2008. In 2009 and 2010, our applications for funding were approved in the amounts of approximately $0.5 million and $0.6 million respectively. We again did not submit an application during 2011 and 2012, and we do not expect to receive any grants during 2013.

In order to meet specified conditions in connection with previous grants and programs of the OCS, we have made representations to the Israel government about our Israeli operations. From time to time the conduct of our Israeli operations has deviated from our forecasts. If we fail to meet the conditions of the grants, including the maintenance of a material presence in Israel, or if there is any material deviation from the representations made by us to the Israeli government, we could be required to refund the grants previously received (together with an adjustment based on the Israeli consumer price index and an interest factor) and would likely be ineligible to receive OCS grants in the future.

Under the Law for the Encouragement of Industrial Research and Development, 5744-1984 and the related regulations, the discretionary approval of an OCS committee is required for any transfer of technology developed with OCS funding, including in the context of certain acquisitions of companies that have received OCS funding, or for the transfer of manufacturing rights outside of Israel. OCS approval is not required for the export of any products resulting from the research and development. There is no assurance that we will receive the required approvals for any proposed future transfer. Such approvals, if granted, may be subject to the following additional restrictions:

- a requirement to pay the OCS a portion of the consideration we receive upon any sale of such technology to an entity that is not Israeli. The scope of the support received, the royalties that were paid by us, the amount of time that elapsed between the date on which the know-how was transferred and the date on which the grants were received, as well as the sale price, will be taken into account in order to calculate the amount of the payment; and

- the transfer of manufacturing rights could be conditioned upon an increase in the royalty rate and payment of increased aggregate royalties (up to 300% of the amount of the grant plus interest, depending on the percentage of the manufacturing that is foreign).

These restrictions may impair our ability to sell certain of our older technology assets outside of Israel. The restrictions will continue to apply even after we repay the full amount of royalties payable for the grants.

You may have difficulties enforcing a U.S. judgment against us and our executive officers and directors or asserting U.S. securities laws claims in Israel.

Commtouch Software Ltd. is organized under the laws of Israel, and we maintain significant operations in Israel. In addition, most of our assets are located outside the United States. Service of process upon our non-U.S. resident directors and enforcement of judgments obtained in the United States against them and Commtouch Software Ltd. may be difficult to obtain within the United States. It may be difficult to assert U.S. securities law claims in original actions instituted in Israel. Israeli courts may refuse to hear a claim based on a violation of U.S. securities laws because Israel is not the most appropriate forum in which to bring such a claim. In addition, even if an Israeli court agrees to hear a claim, it may determine that Israeli law and not U.S. law is applicable to the claim. If U.S. law is found to be applicable, the substance of the applicable U.S. law must be proved as a fact, which can be a time-consuming and costly process. Certain matters of procedure will also be governed by Israeli law. Furthermore, there is little binding case law in Israel addressing these matters.

Israeli courts might not enforce judgments rendered outside Israel which may make it difficult to collect on judgments rendered against us. Subject to certain time limitations, an Israeli court may declare a foreign civil judgment enforceable only if it finds that (a) the judgment was rendered by a court which was, according to the laws of the state of the court, competent to render the judgment; (b) the judgment may no longer be appealed; (c) the obligation imposed by the judgment is enforceable according to the rules relating to the enforceability of judgments in Israel and the substance of the judgment is not contrary to public policy; and (d) the judgment is executory in the state in which it was given.

Even if these conditions are satisfied, an Israeli court will not enforce a foreign judgment if it was given in a state whose laws do not provide for the enforcement of judgments of Israeli courts (subject to exceptional cases) or if its enforcement is likely to prejudice the sovereignty or security of the State of Israel. An Israeli court also will not declare a foreign judgment enforceable if (i) the judgment was obtained by fraud; (ii) there is a finding of lack of due process; (iii) the judgment was rendered by a court not competent to render it according to the laws of private international law in Israel; (iv) the judgment is at variance with another judgment that was given in the same matter between the same parties and that is still valid; or (v) at the time the action was brought in the foreign court, a suit in the same matter and between the same parties was pending before a court or tribunal in Israel.

Provisions of Israeli law may delay, prevent or make difficult an acquisition of Commtouch, which could prevent a change of control and therefore depress the price of our shares.

Israeli corporate law regulates mergers and acquisitions of shares through tender offers, requires special approvals for transactions involving significant shareholders and regulates other matters that may be relevant to these types of transactions. Furthermore, Israeli tax law treats stock-for-stock acquisitions between an Israeli company and a foreign company less favorably than does U.S. tax law. For example, Israeli tax law may subject a shareholder who exchanges his Ordinary Shares for shares in a foreign corporation to immediate taxation or to taxation before his investment in the foreign corporation becomes liquid. These provisions may adversely affect the price of our shares.

As a foreign private issuer whose shares are listed on the NASDAQ Capital Market, we may follow certain home country corporate governance practices instead of certain NASDAQ requirements.

As a foreign private issuer whose shares are listed on the NASDAQ Capital Market, we are permitted to follow certain home country corporate governance practices instead of certain requirements of the NASDAQ Listing Rules.

Among other things, we may follow home country practice with regard to composition of our Board of Directors, or Board, and quorum requirements at shareholders' meetings. In addition, we may follow our home country law, instead

of the NASDAQ Listing Rules, which require that we obtain shareholder approval for certain dilutive events, such as for the establishment or amendment of certain equity based compensation plans, an issuance that will result in a change of control of the Company, certain transactions other than a public offering involving issuances of a 20% or more interest in the Company and certain acquisitions of the stock or assets of another company.

A foreign private issuer that elects to follow a home country practice instead of NASDAQ requirements must submit to NASDAQ in advance a written statement from an independent counsel in such issuer's home country certifying that the issuer's practices are not prohibited by the home country's laws. In addition, a foreign private issuer must disclose in its annual reports filed with the Securities and Exchange Commission or on its website each such requirement that it does not follow and describe the home country practice followed by the issuer instead of any such requirement (see Item 16G. "Corporate Governance" for a list of those home country practices followed by us). Accordingly, our shareholders may not be afforded the same protection as provided under NASDAQ's corporate governance rules.

Item 4. Information on the Company.

Overview

The legal name of the Company is Commtouch Software Ltd., and its principal executive offices are located at 1 Sapir Rd., 5th Floor, Beit Ampa, P.O. Box 4014, Herzliya, 46140 Israel, where our telephone number is 972–9–863–6888. The Company was incorporated as a private company under the laws of the State of Israel on February 10, 1991 and its legal form is a company limited by shares. Commtouch became a public company on July 15, 1999. Its Amended and Restated Articles of Association are on file in Israel with the office of the Israeli Registrar of Companies and available for public inspection at that office. The Company wholly owns the following main subsidiary companies, either directly or through holding companies:

a. Commtouch Inc., a California corporation and a wholly owned subsidiary of the Company, which has its principal office located at 7927 Jones Branch Drive, Suite 2250, Tysons Corner, VA, 22102 where certain members of management and related personnel are located, plus two supporting offices located at 1731 Embarcadero Road, Suite 230, Palo Alto, CA 94303, tel: (650) 864–2000, and 7121 Fairway Dr., Suite 104, Palm Beach Gardens, FL 33418, tel: 561 575-3200. The Company expects to merge the Florida office with its Virginia office later in 2013, terminate its Florida lease and enter into a new lease for expanded space in Virginia.

b. Commtouch Iceland hf, a limited liability company organized and existing under the laws of Iceland and wholly owned by the Company, with an office at Thverholti 18, IS-105, Reykjavik, Iceland, tel: 354-540-7400.

c. eleven Gesellschaft zur Entwicklung und Vermarktung von Netzwerktechnologien mbH, a German limited liability company and owned by the Company through a holding company structure, with an office at Hardenbergplatz 2, 10623, Berlin, Germany, tel: 49 (0)30/52 0056–0.

We are a provider of Internet security technology and cloud-based services comprised of messaging, antivirus and Web security solutions. We provide our services to a wide array of customers and OEM and service provider distribution partners, including network and security vendors offering content security gateways, unified threat management, or "UTM", solutions, network appliances, antivirus solutions and to service providers such as Software-as-a-Service, or SaaS, vendors, Web hosting providers and Internet service providers. Our multiple services are intended to provide Internet security for various users of the Internet against the harmful effects of spam, malevolent software or "malware", unwelcome websites, etc.

Our services include real-time Inbound Anti-Spam, Outbound Spam Protection for service providers, Zero-Hour Virus Outbreak Detection, GlobalView Mail Reputation, Command Antivirus, GlobalView URL Filtering and, more recently, Email Secaas (which is comprised of inbound and outbound anti-spam, plus antivirus) and Email Security On-Premise.

Additional Detail on Our Offerings

Our anti-spam and antivirus services can be accessed through various means, including i) through the integration of a SDK, which, upon integration, is then able to communicate with our worldwide cloud Detection Centers that provide our customers and users with the most up to date protection against the latest Internet threats ii) through our new full

cloud-based Email Secaas service, which is integrated into service providers' existing email infrastructure as an upstream Mail Transfer Agent, or MTA, with incoming email being directed to the Commtouch cloud infrastructure for review, and iii) through "Email Security On-Premise", a solution integrated into service providers' existing e-mail server infrastructure either through integration as an SMTP proxy, or a plug-in via numerous interfaces, including SpamAssassin (spamd) and Sendmail Milter. This on-premise solution also offers GlobalView Mail Reputation services.

Our URL filtering services currently are only offered through a SDK integration, though the Company expects to release a cloud-based Web SaaS service during the second half of 2013.

At the core of our messaging security offerings is our proprietary Recurrent Pattern Detection (RPD)™ technology which, in general terms, analyzes messages associated with mass email outbreaks and directs the blocking of such emails, without the need to analyze individual messages. Outbound Spam Protection is intended to enable service providers to block emails being sent from their system that contain spam, phishing or malware, and identify the source of the problem. Inbound Anti-Spam is intended to enable customers to block their end users' receipt of such unwanted emails. GlobalView Mail Reputation fights unwanted email at a network's perimeter, i.e. fighting them at the entry point, before these messages enter the network, based on identifying characteristics of the source of the email.

At the core of our Web security solutions is our ability to analyze various feeds from worldwide sources, as well as data from our RPD technology, pertaining to URLs, and provide a classification of the URLs based on a set of categories.

At the core of our Command Antivirus solutions is our proprietary detection and remediation technology and unique engine design based on a combination of heuristics, emulation and several types of signatures, as well as an "in the cloud" infrastructure, which allows for a high degree of flexibility for our OEM customers.

In February 2011, we announced the availability of all three of our principal service offerings – messaging, antivirus and Web security – in one unified SDK. The unified SDK can be integrated into the products of security and networking vendors on an OEM basis, as well as into service providers' infrastructure. Typical solutions that would benefit from the unified engine are software or hardware solutions or services that combine multiple security technologies, such as UTM, secure content filtering gateways and SaaS security solutions. The three principal service offerings – messaging, antivirus and Web security – are still available also in non-unified, individual SDKs for our OEM and service provider customers.

In January 2012, we announced the availability of our Mobile Security SDK, providing antivirus and Web security for Android devices.

We also offer the following services typically through reseller channels:

- An enterprise anti-spam and Zero-Hour virus outbreak detection solution, which allows the reseller's customers to download an Enterprise Gateway (a software program) enabling the subject Commtouch services to be provided in real time by our Detection Centers. Through the Enterprise Gateway, messages are filtered at the customer organization's entry point, before being distributed to recipients, with added user-level controls and a top level of secure spam and virus detection services from the Detection Center, all allowing for real-time reaction to worldwide attacks.
- Command Anti-Malware service known as "CSAM", which offer world-class anti-malware protection for consumers and small businesses, as well as enterprises with hundreds of managed endpoints.
- F·PROT Antivirus client for various operation systems directed to consumers and small businesses. The client utilizes signature-based malware detection together with advanced heuristics, and also includes automatic updates to ensure low maintenance.

Sales and Marketing

We utilize third party distribution channels to sell our products. Generally, our SDK is provided to OEM and service provider customers, who in turn integrate the software into their product or service offerings for sale or provision of our services to their customers. We are paid service fees under a variety of fee structures, including fixed fee and fee sharing arrangements.

We anticipate that our Email SecaaS service will be sold primarily through reseller and OEM/service provider channels.

Our enterprise anti-spam and Zero-Hour virus outbreak detection gateway, CSAM antivirus and F-Prot antivirus services, are sold through resellers, who typically pay us pre-negotiated fees after each sale is closed with a reseller's customer.

All Commtouch sales are managed by our Senior Vice President, Worldwide Sales, who is based in our Virginia office and who works closely with our sales teams in Israel, the United States, Europe and Iceland. The Company's marketing efforts are aimed mainly at potential OEM and service provider customers, as well as resellers and distributors. The marketing department is centralized in our subsidiary's Virginia office, though our personnel travel internationally in furtherance of the Company's marketing goals, and we retain marketing personnel in other offices throughout the organization.

Intellectual Property

We regard our patented and patent pending anti–spam and antivirus technology, copyrights, service marks, trademarks, trade secrets and similar intellectual property as critical to our success, and rely on patent, trademark and copyright law, trade secret protection and confidentiality and/or license agreements with our employees, customers, partners and others to protect our proprietary rights.

During 2004, we purchased a United States patent, U.S. Patent No. 6,330,590. During 2005, we filed in the United States an anti-spam related patent application, claiming priority for a prior period based on the filing of U.S. Provisional Patent Application. This application remains outstanding. During 2006, we filed in the United States a patent application relating to the prevention of spam in streaming systems or, in other words, unwanted conversational media sessions (i.e. voice and video related). This provisional application was converted to a formal patent application and, effective December 7, 2010, the United States Patent and Trademark Office split our application into three pending applications and issued us a new patent under the original application – United States Patent No. 7,849,186. In 2011, a divisional patent was issued in connection with one of those split applications – United States Patent No. 7,991,919, which will have a term concurrent with US Patent No. 7,849,186. On May 29, 2012 and on June 5, 2012, two additional divisional patents were issued in connection with the final two split applications – United States Patent No. 8,190,737 and United States Patent No. 8,195,795, respectively, both of which also will have a term concurrent with U.S. Patent 7,849,186. In 2013, we filed in the United States a new application for a patent regarding a unified platform that leverages the various proprietary Internet security tools we employ to resolve security threats. We may seek to patent certain additional software or other technology in the future.

We are actively maintaining our registered trademark for "COMMTOUCH", which is registered in the U.S., Canada, Israel and European Union and China. With the acquisition of certain assets of Authentium during 2010, we also acquired registered trademarks in "Command Antivirus", "Command Anti-Malware", "Command On Demand", "Command Interceptor" and "Galileo", as well as registered service marks in "Authentium" and "Authentium ESP". We are allowing the registration of Command Interceptor to lapse, and may allow others of these trademarks to lapse over time. A previous registration of "PRONTO" in Canada is still in force, but we are not maintaining this registration and it will lapse in 2014. Since at least September 2003, we have claimed trademark rights in "RPD" and "Recurrent Pattern Detection", as applicable to our messaging security solutions. We have also been claiming trademark rights in Zero-Hour in relation to our virus outbreak detection product (and more recently one of our web security products) and GlobalView in relation to our Internet Protocol, or IP, reputation and Web security products, as well as our "cloud computing" network infrastructure.

It may be possible for unauthorized third parties to copy or reverse engineer certain portions of our products or obtain and use information that we regard as proprietary. In addition, the laws of some foreign countries do not protect proprietary rights to the same extent as do the laws of the United States. There can be no assurance that our means of protecting our proprietary rights in the United States or abroad will be adequate or that competing companies will not independently develop similar technology.

Other parties may assert infringement claims against us. We may also be subject to legal proceedings and claims from time to time in the ordinary course of our business, including claims of alleged infringement by us and/or our customers of the trademarks and other intellectual property rights of third parties. Our customer agreements typically include indemnity provisions, so we may be obligated to defend against third party intellectual property rights infringement claims on behalf of our customers. Such claims, even if not meritorious, could result in the expenditure of significant

financial and managerial resources. During 2011, one such indemnification demand was made by a customer, and we continue to cooperate with that customer in seeking to defeat the underlying patent infringement claims. While we believe that adequate non-infringement and/or invalidity arguments exist, we are uncertain if the case will proceed to judgment. During early 2013, we learned that our customer is negotiating a settlement of the matter, and we have been asked to contribute a portion towards the settlement. It is too early in the negotiations process to anticipate the outcome of the settlement negotiations and our possible contribution towards any final settlement.

Government Regulation

Laws aimed at curtailing the spread of spam have been adopted by the United States federal government, i.e. CAN-SPAM Act, and some individual U.S. states, with the CAN-SPAM Act superseding some state laws or certain elements thereof. See also disclosure under "Item 3. Key Information– Risk Factors—Business Risks—"Tighter governmental enforcement of regulations could decrease the distribution of unsolicited bulk (spam) email and malicious software and decrease demand for our solutions, or increase our cost of doing business." Though not totally clear as to the exact reason, approximately two years ago we began to see a gradual decline in the amount of spam traffic on the Internet. While the decrease leveled off last year, any continuation of this trend can have a negative effect our business, as potential customers may not view the need to acquire a robust anti-spam solution with as much urgency, especially if such solution is to replace a third party legacy anti-spam solution.

The propagation of email viruses, whether through email or Web sites, which are aimed at destroying or stealing third party data, is illegal under standard state and federal law outlawing theft, misappropriation, conversion, etc., without the need for special legislation prohibiting such activities on the Internet. Despite the existence of these laws, sources for Internet viruses continue to spread multi-variant viruses seemingly without much fear of recrimination. New laws providing for more stringent penalties could be adopted in various jurisdictions, but it is unclear what, if any, affect these would have on the anti-virus industry in general and our Command Antivirus, F-Prot antivirus, Zero-Hour Virus Outbreak Detection and GlobalView URL filtering solutions in particular.

Employees

As of December 31, 2012, 2011 and 2010, we had 198, 86, and 93 employees, respectively, with such employees being located in our offices in the United States, Israel, Iceland and Germany. As of December 31, 2012, our employees were categorized as follows:

LOCATION	**General & Administrative**	**Sales & Marketing**	**Research & Development**	**Hosting (Operations)**	**TOTAL:**
ISRAEL OFFICE	9	13	37	-	59
U.S. OFFICE:					
California	5	5	-	8	18
Florida	2	2	9	1	14
Virginia	3	8	1	-	12
Iceland	5	5	21	4 (operations and IT)	35
Germany	8	30 (including support)	18	4	60

While employment related issues occasionally arise in the normal course, we believe that, on the whole, relations with our employees are good.

None of our U.S. employees are covered by a collective bargaining agreement, rather they sign individual offer letters of employment that, along with relevant Company policies and an employee handbook, formalize employees' relationship with our U.S. subsidiary.

Israeli law and certain provisions of the nationwide collective bargaining agreements between the Histadrut (General Federation of Labor in Israel) and the Coordinating Bureau of Economic Organizations (the Israeli federation of employers' organizations) apply to Commtouch's Israeli employees. These provisions principally concern the maximum length of the workday and workweek, minimum wages, contributions to a pension fund, insurance for work–related accidents, procedures for dismissing employees, determination of severance pay and other conditions of employment. Furthermore, pursuant to such provisions, the wages of most of Commtouch's Israeli employees are subject to cost of living adjustments, based on changes in the Israeli Consumer Price Index. The amounts and frequency of such adjustments are modified from time to time. Also, all Israeli employees employed for at least a year commencing in 2009 are entitled to the funding of pension benefits by preset monthly contributions of the employee and the employer. Israeli law generally requires the payment of severance pay upon the retirement or death of an employee or upon termination of employment by the employer or, in certain circumstances, by the employee. We currently fund our ongoing severance obligations by making monthly payments for insurance policies and by an accrual. A general practice in Israel followed by Commtouch, although not legally required, is the contribution of funds on behalf of certain employees to an individual insurance policy known as "Managers' Insurance." This policy provides a combination of savings plan, insurance and severance pay benefits to the insured employee. It provides for payments to the employee upon retirement or death and secures a substantial portion of the severance pay, if any, to which the employee is legally entitled upon termination of employment. Each participating employee contributes an amount equal to 5% of such employee's base salary, and the employer contributes between 13.3% and 15.8% of the employee's base salary. Full-time employees who are not insured in this way are entitled to a savings account, to which both the employee and the employer make a monthly contribution of 5% of the employee's base salary. We also provide certain Israeli employees with an Education Fund, to which each participating employee contributes an amount equal to 2.5% of such employee's base salary, and the employer contributes an amount equal to 7.5% of the employee's base salary, up to a certain maximum base salary set by law.

Description of Property

All of our facilities are leased. We recently relocated our Israel and California offices to Herzliya, Israel and Palo Alto, CA, respectively, and we anticipate moving our McLean, VA offices to a nearby location to accommodate our expansion. Certain employees from our Florida office have relocated to our McLean office, and we anticipate closing our Florida office during the third quarter of 2013.

Our office in Herzilya, Israel, is approximately 1,100 square meters and houses research and development, sales, marketing and administrative personnel. Our U.S. subsidiary Commtouch Inc. is headquartered in McClean, VA, in an office of approximately 3,050 square feet (and will grow to approximately 7,022 square feet) and it houses and will house senior management, marketing, Command Antivirus operations (which is being moved from our Florida office), and administrative personnel; and its office in California (approximately 3,332 square feet), is staffed by hosting (operations), sales and administrative personnel. Our subsidiary Commtouch Iceland hf is located in Reykjavik, Iceland in an office of approximately 1,000 square meters, which houses antivirus operations, sales and some administrative personnel. Our subsidiary eleven is based in Berlin, Germany in an office of approximately 960 square meters, which houses research and development, operations, sales, marketing and administrative personnel.

Geographic Information

The Company conducts its business on the basis of one reportable segment in accordance with Accounting Standards Codification™, or ASC, 280, "Segment Reporting".

Revenues for Last Three Financial Years

See Item 5. Operating and Financial Review and Prospects – "Revenue Sources" and the financial statements included elsewhere in this annual report. Below is a breakdown of our revenues by location (in thousands):

	Year December 31,		
	2010	2011	2012
Israel	$ 2,047	$ 2,044	$ 2,541
North America	9,184	12,655	11,847
Europe	4,454	4,869	5,737
Asia	1,976	3,036	3,484
Other	500	412	301
	$ 18,161	$ 23,016	$ 23,910

We made capital expenditures in our cloud infrastructure of approximately $700 during 2012. We have had only negligible capital divestitures in the last three financial years.

Competitive Landscape

The markets in which Commtouch competes are intensely competitive and rapidly changing. However, we believe there are very few competitors that offer the complete package of anti-spam, anti-virus (both traditional and complementary real-time offerings), IP reputation and Web security protections that Commtouch provides.

The principal competitive factors in our industry include price, product functionality, product integration, platform coverage and ability to scale, worldwide sales infrastructure and global technical support. Some of our competitors have greater financial, technical, sales, marketing and other resources than we do, as well as greater name recognition and a larger installed customer base. Additionally, some of these competitors have research and development capabilities that may allow them to develop new or improved products that may compete with product lines we market and distribute, possibly at a lower cost. Our success will depend on our ability to adapt to these competing forces, to develop more advanced products more rapidly and less expensively than our competitors and/or to purchase new products by way of strategic acquisitions, and to educate potential customers as to the benefits of using our products rather than developing their own products.

In the market for messaging security solutions, there are sophisticated offerings that compete with our solutions. Email defense security providers offering forms of software as a service (SaaS), packaged software (gateway), multi-functional appliances and managed service solutions and which may be viewed as both competitors and potential customers to Commtouch include Google (Postini), Symantec (Brightmail), TrendMicro, Intel (McAfee) and Cisco (IronPort). Messaging security providers offering solutions on an OEM basis similar to Commtouch's business model, and which may be viewed as direct competitors, include Cloudmark, Mailshell and Vade Retro.

The market for real-time virus protection products is also constantly evolving, as those designing and proliferating viruses and other malware seek new vulnerabilities and distribution techniques, and also continue to leverage email distribution as a cost-effective medium for accurately targeting broad, numerous potential victims. Commtouch's real-time offering differs from traditional anti-virus solutions (such as our Command Antimalware solution) by leveraging our global footprint and patented RPD technology to rapidly detect outbreaks, often hours or days before traditional antimalware solutions; it thereby offers a complementary solution to signature and heuristic-based anti-virus engines. For this reason, our Zero-Hour virus outbreak protection engine has been deployed by several security companies and service providers.

In the market for antimalware solutions, there are vendors offering fairly effective solutions using various technologies based on signatures, emulation and heuristics. Commtouch distinguishes itself in independent tests of detection capability, has an exclusive OEM/service provider focus, plus an increasing focus on heuristics and zero day effectiveness. Most companies in this space provide end-user products and in some cases make software development kits available on an OEM basis. Competitors to Commtouch include McAfee, Sophos, Kaspersky, and open source software such as Clam-AV.

In the market for Web security solutions, there are advanced offerings that compete with our GlobalView URL filtering solution. Web security providers offering forms of software (gateway), multi-functional appliances and managed service solutions and which may be viewed as both competitors and potential customers to Commtouch include Intel (McAfee), WebSense and BlueCoat. Web security providers offering solutions on an OEM basis similar to Commtouch's business model, and which may be viewed as direct competitors, include Webroot (BrightCloud), Symantec (RuleSpace) and IBM (ISS/Cobion).

We expect that the markets for Internet security solutions will continue to become more consolidated, with companies increasing their presence in this market or entering ancillary markets by acquiring or forming strategic alliances with our competitors or business partners. Some examples of this in the messaging security field are the acquisitions of IronPort by Cisco, McAfee by Intel, both Frontbridge and Sybari Software by Microsoft, and Bizanga by Cloudmark. Some examples of this in the Web security field are the acquisitions of Fastdata by Cisco, SurfControl by WebSense, CipherTrust by Secure Computing, Secure Computing by McAfee, McAfee by Intel, RuleSpace by Symantec and BrightCloud by Webroot.

See also disclosure under "Item 3. Key Information– Risk Factors—Business Risks—We have many established competitors who are offering a multitude of solutions to the problems of spam/virus distribution and Web-related security threats."

Item 4A. Unresolved Staff Comments.

Not applicable.

Item 5. Operating and Financial Review and Prospects.

Overview

From 2003 through 2008, the sole focus of our business had been the development and selling, through reseller and OEM distribution channels, of anti-spam, Zero-Hour virus outbreak detection and IP reputation solutions to a wide array of customers. During late 2008, we expanded our focus by way of the release of our first URL filtering solutions for the web security market. In 2010, we acquired certain assets comprising the Command Antivirus business unit of Authentium, Inc. On October 1, 2012, the company completed the acquisition of the antivirus business of Frisk. The acquisition enables the company to provide antivirus technology utilizing the combined resources of both organizations. It also helps support the launch of a private label antivirus solution for the OEM and service provider markets while also enhancing the company's Saas capabilities. On November 16, 2012 the Company completed the acquisition of eleven. The acquisition of eleven enables Commtouch to accelerate delivery of private label cloud–based security solutions specifically designed for the OEM and service provider markets.

Critical Accounting Policies and Estimates

Operating and Financial Review and Prospects are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. On an ongoing basis, the Company's management evaluates estimates. Such estimates are based on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities.

Accounting for Stock–Based Compensation:

ASC 718 - "Compensation-stock Compensation"ASC 718, requires companies to estimate the fair value of equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company's consolidated income statements.

The Company recognizes compensation expense for the value of its awards on a straight line basis over the requisite service period of each of the awards, net of estimated forfeitures. Estimated forfeitures are based on actual historical pre-vesting forfeitures. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

The Company estimates the fair value of stock options granted using the Black-Scholes option-pricing model. The option-pricing model requires a number of assumptions, of which the most significant are the expected stock price volatility and the expected option term. Expected volatility was calculated based upon actual historical stock price movements. The expected term of options granted represents the period of time that options granted are expected to be

outstanding. The risk-free interest rate is based on the yield from U.S. treasury bonds with an equivalent term. The Company has historically not paid dividends and has no foreseeable plans to pay dividends.

The Company applies ASC 718, and ASC 505-50, "Equity Based Payments to Non Employees", or ASC 505-50, with respect to options issued to non-employees.

The fair value for options granted in 2010, 2011 and 2012 is estimated at the date of grant using a Black-Scholes options pricing model with the following weighted average assumptions:

	Year ended December 31,		
Employee stock options	**2010**	**2011**	**2012**
Volatility	71%-73%	68%-70%	38%-51%
Risk-free interest rate	1.1%-1.6%	0.6%-2.1%	0.5%-0.9%
Dividend yield	0%	0%	0%
Expected life (years)	3.7-4.6	3.6-4.8	3.8-4.9

Revenue recognition

We derive revenues from the sale of real-time Inbound Anti-Spam, Outbound Spam Protection for service providers, Zero-Hour virus outbreak protection, GlobalView Mail Reputation, Command Antivirus, GlobalView URL Filtering and, more recently, Email SecaaS (which is comprised of inbound and outbound anti-spam, plus antivirus) and Email Security On-Premise.

Revenue is recognized when there is a persuasive evidence of an arrangement, the service has been rendered, the collection of the fee is probably and the amount of fees to be paid by the customer is fixed or determinable.

Revenues from such services are recognized ratably over the contractual service term, which generally includes a term period of one to three years.

Deferred revenues include unearned amounts received from customers, but not yet recognized as revenues.

Accounting for Income Tax

We account for income taxes in accordance with FASB ASC 740, "*Income Taxes.*" ASC 740 prescribes the use of the liability method whereby deferred tax assets and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. We record a valuation allowance, if necessary, to reduce deferred tax assets to the amount that we believe is more likely than not to be realized.

Deferred tax assets are classified as current or non-current based on the classification of the related asset or liability for financial reporting, or according to the expected reversal dates of the specific temporary differences if not related to an asset or liability for financial reporting.

ASC 740 contains a two-step approach to recognizing and measuring a liability for uncertain tax positions. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. No liability for unrecognized tax benefits was recorded as a result of the implementation of ASC 740.

Goodwill and Intangible Assets

Goodwill and certain other purchased intangible assets have been recorded as a result of acquisitions made in 2010 and 2012. Goodwill represents the excess of the purchase price in a business combination over the fair value of net tangible and intangible assets acquired. Goodwill is not amortized, but rather is subject to an impairment test. The Company performs an annual impairment test at December 31 of each fiscal year, or more frequently if impairment indicators are present. We operate in one operating segment, and this segment comprises the only reporting unit.

ASC 350 prescribes a two-phase process for impairment testing of goodwill. The first phase screens for impairment, while the second phase (if necessary) measures impairment. Goodwill impairment is deemed to exist if the net book value of a reporting unit exceeds its estimated fair value determined using market capitalization. In such case, the second phase is then performed, and the Company measures impairment by comparing the carrying amount of the reporting unit's goodwill to the implied fair value of that goodwill. An impairment loss is recognized in an amount equal to the excess. For each of the two years in the period ended December 31, 2012, no impairment losses have been identified.

Intangible assets that are not considered to have an indefinite useful life are amortized over their estimated useful lives, which range from 8 to 15 years. Acquired customer contracts and relationships are amortized over their estimated useful lives in proportion to the economic benefits realized. This accounting policy results in accelerated amortization of such customer contracts and relationships arrangements as compared to the straight-line method. Other intangible assets consist primarily of technology, and are amortized over their estimated useful lives on a straight-line basis.

The carrying amount of these assets to be held and used is reviewed whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of these assets is measured by comparison of the carrying amount of each asset (or asset group) to the future undiscounted cash flows the asset (or asset group) is expected to generate. If the asset is considered to be impaired, the amount of any impairment is measured as the difference between the carrying value and the fair value of the impaired asset.

In conjunction with Authentium's sale of its remaining business to a third party and the discontinuation of Authentium, in 2011, the Company wrote off the remaining asset related to covenants not-to-compete in the amount of $502, which was recorded in sales and marketing expenses.

Results of Operations

The following table sets forth financial data for the years ended December 31, 2010, 2011 and 2012 (in thousands):

	2010	2011	2012
Revenues	$ 18,161	$ 23,016	$ 23,910
Cost of revenues	2,918	4,091	4,350
Gross profit	15,243	18,925	19,560
Operating expenses:			
Research and development, net	3,397	5,410	6,281
Sales and marketing	4,575	5,486	5,860
General and administrative	3,911	4,721	6,639
Total operating expenses	11,883	15,617	18,780
Operating income	3,360	3,308	780
Financial income (expenses), net	(55)	(27)	80
Net income before tax benefit	3,305	3,281	860
Tax benefit	(1,098)	(1,317)	(625)
Net income attributable to ordinary and equivalently participating shareholders	$ 4,403	$ 4,598	$ 1,485

Comparison of Years Ended December 31, 2012 and 2011

Revenues. Revenues increased by $0.9 million from $23 million in 2011 to $23.9 million in 2012, which represents a 4% increase. The increase is mainly due to the acquisition and the first consolidation of eleven and Frisk into Commtouch in the fourth quarter of 2012.

Cost of Revenues. Cost of revenues increased by $0.3 million from $4.1 million in 2011 to $4.4 million in 2012, which represents a 6% increase. The increase in 2012 is mainly due to the first consolidation of eleven and Frisk into Commtouch as well as higher facility costs and hosting expenses aimed to serve the increasing number of customers.

Research and Development, net. Research and development expenses increased by $0.9 million and amounted to $6.3 million in 2012 compared to $5.4 million in 2011. $0.7 million out of the total increase is due to the first consolidation of eleven and Frisk in the fourth quarter of 2012 and $0.2 million out of the total increase is due to increase in outside services utilized in 2012.

Research and development expenses in 2012 include $0.2 million of expenses in connection with equity based compensation, compared to $0.3 million of expenses in 2011.

Sales and Marketing. Sales and marketing expenses increased by $0.4 million and amounted to $5.9 million in 2012, compared to $5.5 million in 2011. The increase is mainly due to the first consolidation of Frisk and eleven in the fourth quarter of 2012. Excluding eleven and Frisk, Sales and Marketing payroll increased by $0.3 million in order to expand our existing sales and product marketing resources and rent increased by $0.2 million due to the opening of the new headquarters in Virginia. This increase is offset by a decrease of $0.5 million due to the write off in 2011 of a covenant not to compete asset (acquired in our Authentium acquisition). Sales and marketing expenses in 2012 included $0.2 million expenses in connection with equity based compensation, compared to $0.4 million of expenses in 2011.

General and Administrative. General and administrative expenses increased by $1.9 million, from $4.7 million in 2011 to $6.6 million in 2012. $0.8 million of the total increase is due to acquisition related costs of eleven and Frisk. Salary expenses increased by $0.7 million from $2.8 million in 2011 to $3.5 million in 2012 mainly due to recruitment of additional employees in the Virginia headquarters. Additionally,$0.3 million is due to the first consolidation of Frisk and eleven in the fourth quarter of 2012.

In 2012, general and administrative expenses included $0.8 million expenses in connection with equity based compensation, compared to $0.7 million of expenses in 2011.

Financial Income (Expenses), Net. Financial income (expenses), net, resulted in income of $0.08 million in 2012 compared to expenses of $0.03 million in 2011.

Tax benefit. Tax benefit decreased by $0.7 million from $1.3 million in 2011 to $0.6 million in 2012. In 2012, the deferred tax asset increased by $0.7 million due to an increase in forecasted taxable income that is more likely than not to be realized in the foreseeable future, based on our established pattern of profitability in the last few years resulting, among others, from the new acquisitions that took place in 2012.

Comparison of Years Ended December 31, 2011 and 2010

Revenues. Revenues increased by $4.8 million from $18.2 million in 2010 to $23.0 million in 2011 which represent 27% increase. The increase is mainly due to a growth in market share, an increase in sales derived from our Web security product launched in the fourth quarter of 2008 and sales of the Antivirus product following the purchase of Command Antivirus in September 2010.

Cost of Revenues. Cost of revenues increased by $1.2 million from $2.9 million in 2010 to $4.1 million in 2011 which represents a 40% increase. The increase in 2011 is mainly due to higher facility costs and hosting expenses aimed to serve the increasing number of customers and the Command Antivirus expenses fully consolidated into Commtouch.

Research and Development, net. Research and development expenses increased by $2 million and amounted to $5.4 million in 2011 compared to $3.4 million in 2010. The increase is mainly due to the related Command Antivirus expenses being fully consolidated into Commtouch from September 2010. The increase in our research and development expenses is also due to an OCS grant in 2010, which reduced our payroll cost by $0.8 million, compared to $0 in 2011. Research and development expenses include $0.3 million of expenses in connection with equity based compensation in 2011, compared to $0.3 million of expenses in 2010.

Sales and Marketing. Sales and marketing expenses increased by $0.9 million and amounted to $5.5 million compared to $4.6 million in 2010. The increase is mainly due to the impairment of a covenant not to compete asset (acquired in our Authentium acquisition) in the amount of $0.5 million, increased sales and marketing activity and the related Command Antivirus expenses fully being consolidated into Commtouch beginning in September 2010. Sales and marketing expenses included $0.4 million expenses in connection with ASC 718.

General and Administrative. General and administrative expenses increased by $0.8 million, from $3.9 million in 2010 to $4.7 million in 2011. The increase is mainly due to the update of the earnout liability in the amount of $0.4 million in connection with the acquisition of the assets of the Antivirus business of Authentium Inc. (now known as SafeCentral Inc.) The contingent consideration is subject to adjustments upward or downward based on the revenue derived from the purchased customer contracts and the related Command Antivirus expenses fully being consolidated into Commtouch from September 2010. In 2011, general and administrative expenses included $0.7 million expenses in connection with ASC 718, compared to $0.7 million of expenses in connection with equity based compensation in 2010.

Financial Income (Expenses), Net. Financial income (expenses), net, resulted in expenses of $0.03 million in 2011 compared to expenses of $0.1 million in 2010.

Tax benefit. Tax benefit increased by $0.3 million from $1 million in 2010 to $1.3 million in 2011. In 2011, the deferred tax asset increased by $1.4 million due to an increase in forecasted taxable income that is more likely than not to be realized in the foreseeable future, based on our established pattern of profitability in the last few years.

Quarterly Results of Operations (Unaudited)

The following table sets forth certain unaudited quarterly statements of operations data for the eight quarters ended December 31, 2012. This information has been derived from the Company's consolidated unaudited financial statements, which, in management's opinion, have been prepared on the same basis as the audited consolidated financial statements, and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the information for the quarters presented. This information should be read in conjunction with our audited consolidated financial statements and the notes thereto included elsewhere in this Annual Report. The operating results for any quarter are not necessarily indicative of the operating results for any future period.

Three Months Ended

(in thousands) (unaudited)	Mar 31 2011	June 30 2011	Sep. 30 2011	Dec. 31 2011	Mar 31 2012	June 30 2012	Sep. 30 2012	Dec. 31 2012
Revenues	$ 5,515	$ 5,696	$ 5,855	$ 5,950	$ 5,896	$ 5,671	$ 5,558	$ 6,785
Cost of revenues	1,010	938	1,019	1,124	1,052	1,014	917	1,367
Gross profit	4,505	4,758	4,836	4,826	4,844	4,657	4,641	5,418
Operating expenses:								
Research and development, net	1,247	1,377	1,342	1,444	1,270	1,364	1,462	2,185
Sales and marketing	1,391	1,318	1,138	1,639	1,142	1,288	1,564	1,866
General and administrative	893	1,004	1,209	1,615	1,331	1,384	1,550	2,374
Total operating expenses	3,531	3,699	3,689	4,698	3,743	4,036	4,576	6,425
Operating income	974	1,059	1,147	128	1,101	621	65	(1,007)
Financial income(expenses), net	(14)	(45)	15	(23)	23	64	63	(70)
Net income	960	1,014	1,162	105	1,124	685	128	(1,077)
Taxes on income (tax benefit)	(61)	(401)	275	(1,170)	(85)	(119)	109	(530)
Net income attributable to ordinary and equivalently participating shareholders	$ 1,021	$ 1,415	$ 887	$ 1,275	$ 1,209	$ 804	$ 19	$ (547)
Basic								
Net income per share	$ 0.04	$ 0.06	$ 0.04	$ 0.05	$ 0.05	$ 0.03	$ 0.00	$ (0.02)
Diluted net income per share	$ 0.04	$ 0.06	$ 0.04	$ 0.05	$ 0.05	$ 0.03	$ 0.00	$ (0.02)

New Accounting Pronouncements

In February 2013, the FASB (Financial Acounting Standards Board) issued ASU No. 2013-02, "Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income." Under ASU No. 2013-02, an entity is required to provide information about the amounts reclassified out of Accumulated Other Comprehensive Income, or AOCI by component. In addition, an entity is required to present, either on the face of the financial statements or in the notes, significant amounts reclassified out of AOCI by the respective line items of net income, but only if the amount reclassified is required to be reclassified in its entirety in the same reporting period. For amounts that are not required to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures that provide additional details about those amounts. ASU No. 2013-02 does not change the current requirements for reporting net income or other comprehensive income in the financial statements. ASU No. 2013-02 is effective for the Company as of January 1, 2013. Since this standard only impacts presentation and disclosure requirements, its adoption will not have a material impact on the Company's consolidated results of operations or financial condition.

Liquidity and Capital Resources

As of December 31, 2011 and December 31, 2012, we had approximately $20.9 million and $5 million of cash and cash equivalents, respectively. The decrease is mainly due to net cash used in investing activities in 2012 of $11.2 million, which consisted primarily of the payments for the acquisitions of eleven and Frisk and to a lesser degree due to net cash used in operating activities which amounted to approximately $0.4 million and net cash used in financing activities which was approximately $4.2 million. As of December 31, 2011 and December 31, 2012, we had working capital of $17.3 million and $1.5 million, respectively.

Based on the cash balance at December 31, 2012, current projections of revenues and related expenses, the Company believes it has sufficient cash to continue operations at least through May 2014.

The Company financed its acquisitions of Frisk and eleven from its cash reserves, share capital and future contingent payments ("earnouts") based on related product performance, which may be adjusted upward or downward. In connection with the contingent earn-out consideration which is related to the Frisk acquisition, the Company recorded an estimated amount of $1,037,000 as of the acquisition date. As of December 31, 2012, the fair value of the contingent consideration of $73,000 is presented in short term liabilities, and the fair value of the contingent consideration of $985,000 is presented in long term liabilities.

In connection with the contingent earn-out consideration, derived from the eleven acquisition, the Company recorded an estimated amount of $9,399,000 as of the acquisition date. As of December 31, 2012, the fair value of the contingent consideration of $4,048,000 is presented in short term liabilities, and the fair value of the contingent consideration of $6,409,000 is presented in long term liabilities.

Trends

Several key factors and trends affect the information security market and impact how Commtouch conducts business.

- Information Security Threats Continue to Evolve. These threats, against consumers and organizations of all sizes, drive demand for security offerings from service providers and hardware and software vendors. Examples include high profile hacker groups such as Anonymous targeting businesses and governmental organizations with attacks designed to disrupt access and operations and a wide range of malicious software designed to steal information from or gain control of computing systems.
- Mobility. Mobile computing, using devices such as smartphones and tablets along with hundreds of thousands of Internet-connected mobile applications, is rapidly overtaking traditional personal computing paradigms. The "bring your own device" trend in which organizations allow or encourage employees to access organizational resources and process and store organizational data using their personally-owned devices has become prominent across many geographies and market segments. Meanwhile, Commtouch and other security vendors witnessed a dramatic rise in malware on the Android mobile platform in 2012.
- Cloud-Based Computing. Cloud-based computing, in which consumers or organizations remotely access and leverage computing infrastructure or complete information services via the Internet continues to grow rapidly in today's environment thanks to increased connectivity, mobility and the efficiencies offered by cloud based services. Cloud-based "Security as a Service" includes many of the most rapidly growing sub-segments in the information security market. For instance, industry analysts estimate that the market for cloud-based Secure Web Gateway market has a five year CAGR between 22% and 27%.

Contractual Obligations

The following table summarizes our outstanding contractual obligations as of December 31, 2012 (in thousands):

Contractual Obligation	Payments due by period (USD in thousands)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Operating lease obligation	$ 3,722	$ 1,032	$ 1,788	$ 791	$ 110
Other Long-term liabilities reflected on the Company's Balance Sheet - Accrued severance pay	915	-	-	-	915
Other Long-term asset reflected on the Company's Balance Sheet - severance pay fund	(756)	-	-	-	(756)
Net - severance pay liability	159	-	-	-	159
Earnout obligation	10,457	4,048	6,409	-	-
Total	**$ 14,338**	**$ 5,080**	**$ 8,197**	**$ 791**	**$ 269**

Effective Corporate Tax Rates

The Israeli corporate tax rate was 25% in 2010, 24% in 2011 and 25% in 2012 and onwards.

The Company may currently qualify as an "industrial company" within the definition of the Law for the Encouragement of Industry (Taxation). As such, it may be eligible for certain tax benefits, including, inter alia, special depreciation rates for machinery, equipment and buildings, amortization of patents, certain other intangible property rights and deduction of share issuance expenses.

As of December 31, 2012, the Company's net operating loss carryforwards for tax purposes amounted to approximately $ 70,008,000 (including capital loss carryforward of $15,659,000) which may be carried forward and offset against taxable income in the future, for an indefinite period.

As of December 31, 2012, for federal income tax purposes, the U.S. subsidiary had net operating loss carryforwards of approximately $91,755,000 (including capital loss carryforwards of $1,700,000). These losses may offset any future U.S. taxable income of the U.S. subsidiary and will expire in the years 2012 through 2025.

Utilization of U.S. net operating losses may be subject to substantial annual limitation due to the "change in ownership" provisions of the Internal Revenue Code of 1986 and similar state provisions. The annual limitations may result in the expiration of net operating losses before utilization.

Management currently believes that since the Company has a history of losses, and uncertainty with respect to future taxable income, it is more likely than not that some of the deferred tax assets regarding the loss carryforwards will not

be utilized in the foreseeable future. Thus, a valuation allowance was provided to reduce deferred tax assets to their realizable value.

Impact of Inflation and Currency Fluctuations

The currency of the primary economic environment in which the operations of Commtouch and certain subsidiaries are conducted is the U.S. dollar ("dollar"); thus, the dollar is the functional currency of Commtouch and certain subsidiaries.

Commtouch and certain subsidiaries' transactions and balances denominated in dollars are presented at their original amounts. Non-dollar transactions and balances have been remeasured to dollars in accordance with ASC 830, "Foreign Currency Matters". All transaction gains and losses from remeasurement of monetary balance sheet items denominated in non-dollar currencies are reflected in the statements of income as financial income or expenses, as appropriate.

For those subsidiaries whose functional currency has been determined to be their local currency, assets and liabilities are translated at year-end exchange rates and statement of income items are translated at average exchange rates prevailing during the year. Such translation adjustments are recorded as a separate component of accumulated other comprehensive income (loss) in shareholders' equity.

Most of our sales are in U.S. dollars, and the rest are mainly in Euros. However, a portion of our costs relate to our operations in Israel. A substantial portion of our operating expenses in Israel, primarily our research and development expenses are denominated in NIS. Costs and revenues not denominated in U.S. dollars are re-measured to U.S. dollars, when recorded, at prevailing rates of exchange. This is done for the purposes of our financial statements and reporting. As a result, we are exposed to risk to the extent that the value of the U.S. dollar decreases against the NIS. In that event, the U.S. dollar cost of our operations will increase and our U.S. dollar-measured results of operations will be adversely affected. dollar cost of our operations. Also, in the event that the U.S. dollar appreciates against the Euro, our revenues will decrease. Consequently, we are and will be affected by changes in the prevailing NIS/U.S. dollar and Euro/ U.S. dollar exchange rates.

The annual rate of deflation in Israel was 1.7% in 2012, 4% in 2011 and 2.7% in 2010. The NIS appreciated against the U.S. dollar by approximately 2% in 2012, 8% in 2011 and 6% in 2010. The representative dollar exchange rate for converting the NIS to U.S. dollars, as reported by the Bank of Israel, was NIS 3.733 for one U.S. dollar on December 31, 2012. The representative dollar exchange rate was NIS 3.629 on April 22, 2013. Because exchange rates between the NIS and the dollar fluctuate continuously, exchange rate fluctuations and especially larger periodic devaluations will have an impact on our operating results and period–to–period comparisons of our results. The effects of foreign currency re–measurements are reported in the consolidated financial statements for relevant periods in the statement of operations.

Item 6. Directors, Senior Management and Employees.

The following table presents information with respect to our directors' beneficial ownership of our Ordinary Shares as of March 1, 2013. Beneficial ownership is determined in accordance with the rules of the SEC and includes voting or investment power, with respect to shares. To our knowledge, except under applicable community property laws or as otherwise indicated, the persons named in the table have sole voting and sole investment control and rights to receive economic benefits with respect to all shares beneficially owned. The applicable percentage of ownership for each director is based on 26,061,383 Ordinary Shares outstanding as of March 1, 2013. Ordinary Shares issuable upon the exercise of options and other rights, which are exercisable on or within sixty days of March 1, 2013, are deemed outstanding for the purpose of computing the percentage ownership of the director holding those options and other rights.

Name and Position	Age	Percentage of Ordinary Shares Beneficially Owned	Number of Ordinary Shares Beneficially Owned	Number of Options and Warrants included in Beneficial Ownership
Lior Samuelson, Director and Chairman of the Board	63	1.2%	180,000	141,551 options, at exercise prices ranging from $3.18 to $3.47 per Ordinary Share. Expiration dates range from 8/2/16 to 12/13/18.
Aviv Raiz, Director (3)	54	21.3%	5,561,068	75,199 options, at exercise prices ranging from $1.58 to $6.60 per Ordinary Share. Expiration dates range from 12/14/13 to 12/13/18.
Hila Karah, Director (1)(3)	44	<1%		
Shlomi Yanai, CEO and Director	42	<1%		
Yair Shamir, Director (Outside Director) (1)(2)(3)(4)(5)	68	5.5%	1,437,995	108,532 options, at exercise prices ranging from $1.58 to $4.10. Expiration dates range from 3/31/14 to 12/13/18.
Yair Bar-Touv, Director (Outside Director) (1)(2)(3)	52	<1%		
Todd Thomson (2)	52	<1%		
James Hamilton (1)(2)(6)	49	<1%		

(1) Member of the Compensation Committee

(2) Member of the Audit Committee

(3) Member of the Nominating Committee

(4) Mr. Shamir's ownership interest includes 1,264,023 of the Company's Ordinary Shares purchased by Catalyst Private Equity Partners II, for which Mr. Shamir has acted as chairman and managing partner. Mr. Shamir's options, as noted in the table above, are also held on behalf of Catalyst.

(5) Due to Mr. Shamir's acceptance of a position in the new government of the State of Israel, he resigned his position as outside director of the Company effective April 17, 2013. The Company intends to seek the appointment of a new outside director as soon as possible and prior to the lapse of the 90 day period from Mr. Shamir's resignation.

(6) With the departure of Mr. Shamir from the Board, Mr. Hamilton has been appointed to the Audit and Compensation Committees, and Mr. Bar-Touv has joined the Nominating Committee.

Other Senior Management Employees:

The following table sets forth the names and positions of our senior management employees, with ownership data being as of March 1, 2013:

Name	Age	Ownership	Position
Brian Briggs (2)	46	(1)	Chief Financial Officer
Gary Davis	51	(1)	Vice President, General Counsel and Corporate Secretary
Haniel Ilouz	42	(1)	Vice President, Global Engineering
Uri Gal	61	(1)	Global Vice President, Human Resources
Brett Wilson	44	(1)	Vice President, Products and Marketing
Pete Shah	44	(1)	Senior Vice President, Worldwide Sales

(1) less than 1%

(2) Executive Officer, along with Shlomi Yanai, for purposes of the aggregation of compensation and share ownership of major shareholders, directors and executive officers, as appearing elsewhere in this Annual Report

Lior Samuelson has been a member of the Board since August 2010 and has held the position of Chairman of the Board since December 2010. Mr. Samuelson is the founder and managing partner of Mercator Capital, a merchant bank specializing in advising and investing in the technology and telecom sectors. During his extensive career, Mr. Samuelson served as chairman, CEO and board member of several companies focused on technology, telecom, financial services and management consulting. In 2008, he was the chairman of Deltathree (DDDC); from 1997 to 1999, he was the president and CEO of PricewaterhouseCoopers Securities. Prior to that, he was the president and CEO of The Barents Group, a merchant bank specializing in advising and investing in companies in emerging markets. He previously was a managing partner with KPMG and held a senior management position at Booz, Allen & Hamilton. Mr. Samuelson earned B.S. and M.S. degrees in Economics from Virginia Tech.

Aviv Raiz has served as a Director since December 2005. He is the founder and president of Eurotrust Ltd., a company specializing in enterprise level foreign exchange transactions. Mr. Raiz has been active in the foreign exchange markets for over twenty years, and has been a private equity investor in several high-tech, bio-tech and Internet companies. He holds an M.B.A. from Tel Aviv University.

Hila Karah joined the Board of Directors in March 2008. Ms. Karah has been the CIO of Eurotrust Ltd. since 2006, and has been a private and public equity investor in several high-tech, bio-tech and Internet companies since 2000. Prior to joining Eurotrust, Ms. Karah served as a partner financial analyst at Perceptive Life Sciences Ltd., a New York-based hedge fund. Prior to her position at Perceptive, Ms. Karah was a research analyst at Oracle Partners Ltd., a health care-focused hedge fund based in Connecticut. Ms. Karah holds a B.A. in Molecular and Cell Biology from the University of California, Berkeley, and has studied at the [UCB-UCSF JMP].

Yair Shamir joined the Board of Directors as an Outside Director under the Israel Companies Law in March 2008. Mr. Shamir has recently accepted a position in the new Israeli government, and has resigned from the Board effective April 17, 2013. Mr. Shamir has been the Chairman and Managing Partner of Catalyst Investments, and the Chairman of IAI, Israeli Aerospace Industries. From 2004 to 2005, Mr. Shamir was Chairman of El Al, Israeli Airlines and lead the privatization process of the firm. From 1997 to 2005, Mr. Shamir served as Chairman and CEO of VCON Telecommunications Ltd. From 1995 to 1997, Mr. Shamir served as executive vice president of the Challenge Fund-Etgar L.P. From 1994 to 1995, he served as Chief Executive Officer of Elite Food Industries, Ltd. From 1988 to 1993, Mr. Shamir served as Executive Vice President and General Manager of Scitex Corporation, Ltd. Mr. Shamir served in the Israeli Air Force as a pilot and commander from 1963 to 1988. During his term in the Israeli Air Force, Mr. Shamir attained the rank of colonel and served as head of the electronics department, the highest professional electronics position within the Israeli Air Force. He currently serves as a director of DSP Group Corporation, and also serves as director of other private hi-tech companies. Mr. Shamir holds a B.Sc. Electronics Engineering from the Technion, Israel Institute of Technology.

Yair Bar-Touv joined the Board of Directors as an Outside Director under the Israel Companies Law in March 2008. Mr. Bar-Touv previously served as the CIO of a leading government enterprise specializing in analytic software solutions for knowledge discovery (text and data mining) of large volumes of data, with a focus on changing the ways enterprise organizations make decisions with regards to primary business processes. Mr. Bar-Touv is also the former CEO of Elron Telesoft and co-CEO of NCC, a leading Systems Integrator operating in Israel and the USA, which was acquired in 1997 by Elron Electronics. Mr. Bar-Touv holds an M.Sc. in Computer Engineering from the Technion Institute of Technology and a B.Sc. in Electronic Engineering from Ben-Gurion University.

Todd Thomson joined the Board of Directors in November 2011. Mr. Thomson is currently the chairman of Dynasty Financial Partners, a firm dedicated to providing investment and technology platforms to independent advisors. Mr. Thomson is also the founder & CEO of Headwaters Capital, a proprietary investment business and strategic consulting firm. From 1998 through 2007, Mr. Thomson served in top management positions at Citigroup, including as CFO of Citigroupand as CEO of the Global Wealth Management division of Citigroup. Prior to joining Citigroup, Mr. Thomson held senior positions at GE Capital, Barents Group and Bain & Co. Mr. Thomson is also a member of the board of directors of Cordia Bancorp, Bank of Virginia and the World Resources Institute. Mr. Thomson is also a chairman of the Wharton Leadership Advisory Board and was formerly a member of the Board of Trustees of Davidson College. Mr. Thomson received his M.B.A., with distinction, from the Wharton School of Business and his B.A. in Economics from Davidson College.

James Hamilton joined the Board of Directors in February 2012. Mr. Hamilton has been in the technology industry for 26 years and is currently CEO of CPSG Partners, a professional services and consulting company based in Houston. During the past eleven years, he has provided services to security-focused companies, including TippingPoint, Inc., an industry-leading provider of network-based Intrusion Prevention Systems, where he served as President and CEO. [TippingPoint was acquired by 3Com in January of 2005.] Mr. Hamilton also spent two years at SafeNet as EVP of Corporate Development, leading M&A and Strategic Alliances. Additionally, he served as President and CEO of Efficient Networks (acquired by Siemens, Inc. in 2001), after running both global sales and product teams as COO, and also held executive positions with Picazo Communications (acquired by Intel in 1998), Compaq, Networth (acquired by Compaq in 1995), 3Com and Grid Systems. Mr. Hamilton holds a B.Sc. from Lawrence Technical University.

Shlomi Yanai became the CEO of Commtouch in October 2011 and joined the Board of Directors in December 2012. He brings over two decades of experience in the information security industry to the Company. He was previously the vice president of corporate development strategy at SafeNet, a global leader in information security, where he led SafeNet's strategic decisions regarding product and solution partnerships, as well as mergers and acquisitions. Mr. Yanai also served as the vice president for the rapidly-growing authentication business unit and award-winning two-factor authentication solutions at SafeNet, Inc. and Aladdin Knowledge Systems, which merged with SafeNet. Prior to Aladdin, Mr. Yanai managed the product team of BMC Software's security division, specializing in identity and password management systems. Mr. Yanai holds a B.Sc. in mathematics and computer science and an M.B.A from Ben Gurion University in Israel.

Brian Briggs joined Commtouch in January 2013 as its Chief Financial Officer, bringing more than 22 years of finance and operations experience in building and growing profitable companies. Prior to Commtouch, Mr. Briggs served as executive vice president and CFO at SecureNet Payment Systems, a payment processing technology provider. Prior to his post at SecureNet, Mr. Briggs served in various management roles at Custom Direct, Ashton-Potter, Ithaca Bancorp (now M&T Bank), and Ernst & Young. He has earned a degree in finance and economics from Cornell University and completed executive education programs at Harvard Business School, The Wharton School, University of Pennsylvania, Stanford Graduate School of Business and Johnson School of Business – Cornell.

Gary Davis joined Commtouch in September 1999 and he currently serves as Vice President, General Counsel and Corporate Secretary. Mr. Davis has over 25 years of legal experience in both private law firm and corporate practices. Mr. Davis is certified to practice law in both the State of Israel and California. Prior to September 1999, Mr. Davis was in–house counsel to Israel Military Industries and Elta Electronics Industries. He received a B.A. in Political Economy of Industrial Societies from U.C. Berkeley and a J.D. from Golden Gate University.

Pete Shah joined Commtouch in June 2012 as Senior Vice President, Worldwide Sales. He is responsible for leading Commtouch's global field organization in exceeding customer expectations and driving business in both new and existing markets. In addition, Mr. Shah serves as an advisor to Acceleprise, an enterprise technology accelerator

focused on helping early stage technology companies. Before joining Commtouch, Mr. Shah held senior executive leadership positions with InfoVista, as senior vice president of worldwide field operations and at Telarix, as vice president of worldwide sales. In years prior, he held various sales management positions with Portal Software/Oracle, Lawson Software/Infor and Automatic Data Processing (ADP). Mr. Shah holds a B.Sc degree in International Marketing from Penn State University.

Haniel Ilouz joined Commtouch in April 2012 as Vice President, Global Engineering, overseeing Commtouch's research and development department globally. Mr. Ilouz has over 14 years of software development experience, including extensive experience in the management of large global engineering teams. Prior to joining Commtouch, Mr. Ilouz was the research and development director at HP Software, with overall responsibility for planning, design, implementation and maintenance of the Business Service Management Platform and Service Intelligence products. At HP, Mr. Ilouz drove the release of several new products while overseeing a team of over 140 engineers spread across several countries. Before HP, Mr. Ilouz was the research and development manager of SiteScope at Mercury Interactive, which was acquired by HP. He holds a B.A. in Computer Science and Mathematics from the Hebrew University of Jerusalem.

Brett Wilson joined Commtouch in April 2012 as Vice President, Products, and recently has also assumed the role as acting VP, Marketing. Mr. Wilson has more than 20 years of technology and communications experience, including more than 10 years of experience in the information security industry. Before joining Commtouch, Mr. Wilson led portfolio management across product lines and drove multiple technology and service initiatives as vice president of product strategy for Trustwave. He subsequently restructured Trustwave's strategic and tactical partnering approaches as vice president of global channels and business development. Mr. Wilson also led product management, global business development and EMEA sales and marketing for Breach Security. He has also held business development, product management, strategy, and operations roles at Symantec. Prior to joining the information security industry, Brett was a technology policy lobbyist for Rockwell International and a market strategy consultant serving Bell Operating Companies. Mr. Wilson has a B.A. from Cornell University and an M.B.A. from the University of Maryland.

Uri Gal joined Commtouch in February 2013 as Global Vice President, Human Resources. Mr. Gal has more than 20 years of human resources and administration experience and has had success in building and supporting the ever-changing needs of growing and profitable technology companies. Prior to joining Commtouch, Mr. Gal served as global vice president of human resources and administration for Nilit, an industrial company with over 1,500 employees worldwide. Before Nilit, he served as Global VP of human resources in various management roles at Oridion, a globally active medical device company, Comverse, a software and systems company for business enablement, and DHL International. Mr. Gal earned a degree in Behavioral Sciences from Haifa University in Israel, and completed high level human resources executive courses in the United States and at the Israeli Institute.

To the best of our knowledge, there no arrangements or understandings with major shareholders, customers, suppliers or others pursuant to which any person referred to above was selected as a director or member of senior management.

Election of Directors

Directors (other than outside directors, as explained below) are elected by shareholders at the annual general meeting of the shareholders and hold office until the next annual general meeting following the general meeting at which such director is elected and until a successor is elected, or until the director is removed. An annual general meeting must be held at least once in every calendar year, but not more than fifteen months after the preceding annual general meeting. Directors may be removed and other directors may be elected in their place or to fill vacancies in the Board of Directors at any time by the holders of a majority of the voting power at a general meeting of the shareholders. Until a vacancy is filled by the shareholders, the Board of Directors may appoint new directors temporarily to fill vacancies on the Board of Directors. The Amended and Restated Articles of Association of Commtouch authorize the shareholders to determine, from time to time, the number of directors. The maximum number of directors is currently fixed at ten directors, though only seven directors are currently serving on the Board of Directors. There are no family relationships among any of the directors, officers or key employees of Commtouch.

Alternate Directors

The Amended and Restated Articles of Association of Commtouch provide that any director may appoint another person to serve as an alternate director and may remove such alternate. Any alternate director possesses all the rights and obligations of the director who appointed him, except that the alternate has no standing at any meeting while the appointing director is present, the alternate may not in turn appoint an alternate for himself (unless the instrument appointing him otherwise expressly provides) and the alternate is not entitled to remuneration. A person who is not qualified to be appointed as a director may not be appointed as an alternate director, and a person who is not qualified to be appointed as an outside or independent director may not be appointed as an alternate director for an outside or independent director, respectively. Unless the appointing director limits the time or scope of the appointment, the appointment is effective for all purposes until the appointing director ceases to be a director or terminates the appointment. The appointment of an alternate director does not in itself diminish the responsibility of the appointing director as a director. No director has appointed, and, to our knowledge, no director currently intends to appoint, any other person as an alternate director.

Chairman of the Board

Under the Companies Law, the general manager of a company (or a relative of the general manager) may not serve as the chairman of the board of directors, and the chairman of the board of directors (or a relative of the chairman of the board of directors) may not serve as the general manager, unless approved by the shareholders by a special majority vote prescribed by the Companies Law. In any event, the shareholder vote cannot authorize the appointment for a period longer than three years, which period may be extended from time to time by the shareholders with a similar special majority vote. The chairman of the board of directors shall not hold any other position with the company (except as general manager if approved in accordance with the above procedure) or in any entity controlled by the company, other than as chairman of the board of directors of a controlled entity, and the company shall not delegate to the chairman duties that, directly or indirectly, make him or her subordinate to the general manager.

Independent and Outside Directors

A. Under the Israel Companies Law:

The Israel Companies Law requires Israeli companies with shares that have been offered to the public in or outside of Israel to appoint at least two outside directors. No person may be appointed as an outside director if the person or the person's relative, partner, employer or any entity under the person's control has or had, on or within the two years preceding the date of the person's appointment to serve as outside director, any affiliation with the company or any entity controlling, controlled by or under common control with the company. The term affiliation includes:

- an employment relationship;
- a business or professional relationship maintained on a regular basis;
- control; and
- service as an office holder.

No person may serve as an outside director if the person's position or other business activities create, or may create, a conflict of interest with the person's responsibilities as an outside director or may otherwise interfere with the person's ability to serve as an outside director. If, at the time outside directors are to be appointed, all current members of the Board of Directors are of the same gender, then at least one outside director must be of the other gender. At least one of the outside directors is required to have "financial and accounting expertise," unless another member of the audit committee, who is an independent director under the NASDAQ Listing Rules, has "financial and accounting expertise," and the other outside director or directors are required to have "professional expertise," all as defined under the Israel Companies Law. However, if at least one of our other directors (i) meets the independence requirements under the Exchange Act, (ii) meets the standards of the NASDAQ Listing Rules for membership on the audit committee, and (iii) has accounting and financial expertise as defined under Israeli law, then neither of our outside directors is required to possess accounting and financial expertise as long as both possess other requisite professional qualifications.

Outside directors are to be elected by a majority vote at a shareholders' meeting, provided that either:

- such majority includes a majority of the shares held by non–controlling shareholders and shareholders who have no personal interest in the election of the outside directors (excluding a personal interest that is not related to a relationship with the controlling shareholders) who are present and voting at the meeting; or
- the total number of shares held by non–controlling shareholders and disinterested shareholders voting against the election of the director at the meeting does not exceed two percent of the aggregate voting rights in the company.

The initial term of an outside director is three years and may be extended for up to two additional periods of three years each. An outside director may be reelected by our shareholders for such additional periods of up to three years each only if (1) the audit committee and the Board of Directors, in nominating the outside director, confirms that, in light of the outside director's expertise and special contribution to the work of the board of directors and its committees, the reelection for such additional period(s) is beneficial to us, and the election was approved by the majority of shareholders required to appoint external directors for their initial term; or (2) a shareholder holding 1% or more of the voting rights proposed the reelection of the nominee, and the reelection is approved by a majority of the votes cast by the shareholders of the company, excluding the votes of controlling shareholders and those who have a personal interest in the matter as a result of their relations with the controlling shareholders, provided that the aggregate votes cast in favor of the reelection by such non-excluded shareholders constitute more than 2% of the voting rights in the company.

Outside directors may be removed only by the same percentage of shareholders as is required for their election, or by a court, and then only if the outside director ceases to meet the statutory qualifications for their appointment or if they violate their fiduciary duty to the company. Each committee of a company's Board of Directors must include at least one outside director and both the audit committee and compensation committee, the existence of which is required under the Israel Companies Law, must include all outside directors.

An outside director is entitled to compensation as provided in the regulations adopted under the Israel Companies Law and is otherwise prohibited from receiving any other compensation, directly or indirectly, in connection with service provided as an outside director.

As noted previously, due to Mr. Shamir' recent resignation, Mr. Bar-Touv is our only outside director. The Company intends to seek shareholder approval for the appointment of a new outside director as soon as possible and prior to the lapse of 90 days period from Mr. Shamir's resignation.

B. Under Nasdaq and SEC Rules and Regulations:

In addition, the NASDAQ Listing Rules currently require Commtouch to have at least a majority of independent directors, as defined under Listing Rule 5605(a)(2), on the Board and to maintain an audit committee of at least three members, each of whom must:

(i) be independent as defined under Listing Rule 5605(a)(2);

(ii) meet the criteria for independence set forth in Rule 10A-3(b)(1) under the Securities Exchange Act of 1934, as amended, or "Exchange Act", as set forth below (subject to the exemptions provided in Exchange Act Rule 10A-3(c));

(iii) not have participated in the preparation of the financial statements of the Company or any current subsidiary of the Company at any time during the past three years; and

(iv) be able to read and understand fundamental financial statements, including a company's balance sheet, income statement and cash flow statement.

Under limited circumstances, the Company may have one audit committee member not independent in accordance with the above, but such a member would only be able to serve for a maximum of two years.

Exchange Act Rule 10A-3(b)(1) requires that members of the audit committee meet that rule's definition of independence, which requires that an audit committee member may not, except in his or her capacity as a director or committee member, (i) accept directly or indirectly any consulting, advisory, or other compensatory fee from the Company or any of its subsidiaries (except for fixed amounts of compensation under a retirement plan for prior service with the Company, provided that such compensation is not contingent in any way on continued service), and (ii) be an "affiliated person" of the Company or any of its subsidiaries.

NASDAQ rules also require that the Company certify that it has, and will continue to have, at least one member of the audit committee who has past employment experience in finance or accounting, requisite professional certification in accounting, or any other comparable experience or background which results in the individual's financial sophistication, including being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities. Also, the Company is required to disclose whether or not it has an "audit committee financial expert" on its audit committee, as defined under Item 16A to Form 20-F.

The three directors who serve on our audit committee, Mr. Bar-Touv, Mr. Thompson and Mr. Hamilton, qualify as independent directors under NASDAQ Listing Rules (including Exchange Act Rule 10A-3) and further qualify to act as members of our audit committee under the Israel Companies Law.

The Company has identified the following Board members as "Independent directors" pursuant to NASDAQ Listing Rule 5605(a)(2):

a. Yair Bar-Touv
b. Aviv Raiz
c. Hila Karah
d. Todd Thomson
e. James Hamilton

Pursuant to the Israeli Companies Law, an Israeli company, whose shares are publicly traded, may elect to adopt a provision in its articles of association pursuant to which a majority of its board of directors (or a third of its Board of Directors in case the company has a controlling shareholder) will constitute individuals complying with certain independence criteria prescribed by the Israel Companies Law, as well as certain other recommended corporate governance provisions. We have not included such a provision in our articles of association since our board of directors complies with the independence requirements of the NASDAQ and Securities and Exchange Commission regulations described above.

Audit Committee

As noted above in the discussion under "*Independent and Outside Directors*", the Israel Companies Law requires public companies to appoint an audit committee. The audit committee's duties include providing assistance to the board of directors in fulfilling its legal and fiduciary obligations in matters involving our accounting, auditing, financial reporting, internal control and legal compliance functions. In this respect the audit committee approves the services performed by our independent registered public accounting firm and reviews their reports regarding our accounting practices and systems of internal accounting controls. The audit committee also oversees the audits conducted by our independent registered public accounting firm and takes those actions as it deems necessary to confirm that the accountants are independent of management. Under the Israeli Companies Law, the audit committee also is required to monitor whether there are any deficiencies in the administration of our company, including by consulting with the internal auditor and independent registered public accounting firm, to review, classify and approve related party transactions and extraordinary transactions, to review the internal auditor's audit plan and to establish and monitor whistleblower procedures.

An audit committee must consist of at least three directors meeting the independence standards under NASDAQ Listing Rules.

Under the Israel Companies Law, all outside directors must serve on the audit committee, and in any case it must include a majority of independent directors. One of the outside directors must serve as the chair of the audit committee. Furthermore, under the Israel Companies Law, the audit committee may not include the chairman of the board, or any director employed by the Company, by a controlling shareholder or by any entity controlled by a controlling shareholder, or any director providing services to us, to a controlling shareholder or to any entity controlled by a controlling shareholder on a regular basis, or any director whose income is primarily dependent on a controlling shareholder, and may not include a controlling shareholder or any relatives of a controlling shareholder. Under the Companies Law, a meeting of the audit committee is properly convened if a majority of the committee members attend the meeting, and such majority includes at least one outside director. Individuals who are not permitted to be audit committee members may not participate in the committee's meetings other than to make a presentation regarding a particular issue. However, an employee who is not a controlling shareholder or relative may participate in the

committee's discussions but not in any vote, and the company's legal counsel and corporate secretary may participate in the committee's discussions and votes if requested by the committee.

Compensation Committee

On December 12, 2012, Amendment 20 to the Israel Companies Law, or "Amendment 20", came into force, and its provisions are summarized below:

All public companies and bond companies are required to establish a compensation committee, with one member of serving as chairman of the committee. The committee is to be made up of at least three directors, with a majority of outside directors. The remaining directors shall be directors who do not receive direct or indirect compensation for their role as directors (other than compensation paid or given in accordance with Israeli Companies Law regulations applicable to the compensation of external directors, or amounts paid pursuant to indemnification and/or exculpation contracts or commitments and insurance coverage). The compensation committee may not include the chairman of the board, any director employed by or otherwise providing services on a regular basis to the Company, to a controlling shareholder or to any entity controlled by a controlling shareholder, any director whose main livelihood is dependent on a controlling shareholder, or a controlling shareholder or a relative thereof. The committee is responsible for (i) proposing an office holder compensation policy to the Board of Directors, (ii) proposing necessary revisions to the compensation policy and examining its implementation, (iii) determining whether to approve transactions with respect to compensation of office holders, and (iv) determining, in accordance with our office holder compensation policy, whether to exempt the compensation terms with an unaffiliated nominee for the position of chief executive officer from requiring shareholders' approval, provided such terms meet with the company's compensation policy.

"Say before pay" rules: The compensation policy recommended by the compensation committee is to be approved by the Board and then, before it takes effect, by shareholders in a non-binding vote by the affirmative vote of a majority of the shares voting on the matter, provided that (i) such majority includes at least a majority of the shares of shareholders who are non-controlling shareholders and do not have a personal interest in the said resolution; or (ii) the total number of shares of shareholders specified in clause (i) who voted against this resolution does not exceed 2% of the voting rights in the Company. If the shareholders do not approve the policy, the policy will be returned for further deliberation by the Board, taking into account the rejection of the policy by the minority shareholders. The Board may ultimately approve the policy despite the minority's disapproval, if it finds that the policy is in the company's best interest. The compensation policy must be approved at least every three years. The Board is required to reevaluate the policy from time to time and if a material change occurs.

Prior to the effectiveness of Amendment 20, a compensation committee already existed and was responsible for formulating the Company's executive compensation policies. This committee will continue to function under the guidelines of the new law. As of the date of the filing of this Annual Report, the Company had not yet adopted a compensation policy. The deadline under Israeli law for completing the compensation policy adoption process is September 12, 2013. In the interim period until the adoption of the compensation policy, the approval of office holder compensation, other than the CEO and directors, requires compensation committee and Board approval, which must take into account certain consideration enumerated in the new law. If the compensation committee determines that a compensation arrangement constitutes an immaterial amendment to an existing compensation arrangement of an officer who is not a director, the approval of the compensation committee without Board approval is sufficient. Any changes in CEO or director compensation during this interim period require shareholder approval by a special majority.

The Compensation Committee is also responsible for administering the Company's various stock option plans, including the issuance of option grants to employees of the Company and its subsidiaries.

Nominating Committee

The committee's responsibilities include identifying individuals qualified to become board members and recommending director nominees to the board.

Internal Auditor

Under the Israel Companies Law, the Board of Directors must appoint an internal auditor, nominated by the audit committee. The role of the internal auditor is to examine, among other matters, whether a company's actions comply with relevant law and orderly business procedure. Under the Israel Companies Law, the internal auditor may be an employee of the company but not an interested party or office holder, or a relative of an interested party or office

holder, and he or she may not be the company's independent accountant or its representative. The Company routinely engages an Internal Auditor who is an independent third party.

Approval of Certain Transactions; Obligations of Directors, Officers and Shareholders

The Israel Companies Law codifies the fiduciary duties that office holders, including directors and executive officers, owe to a company. An office holder's fiduciary duties consist of a duty of care and a duty of loyalty. Each person listed in the first table that appears above at the beginning of this Item 6 is an office holder.

The duty of loyalty requires an office holder to act in good faith and for the benefit of the company, including to avoid any conflict of interest between the office holder's position in the company and such person's personal affairs, avoiding any competition with the company, avoiding exploiting any corporate opportunity of the company in order to receive personal advantage for such person or others, and revealing to the company any information or documents relating to the company's affairs which the office holder has received due to his or her position as an office holder. A company may approve any of the acts mentioned above provided that all the following conditions apply: the office holder acted in good faith and neither the act nor the approval of the act prejudices the good of the company, and the office holder disclosed the essence of his personal interest in the act, including any substantial fact or document, a reasonable time before the date for discussion of the approval. A director is required to exercise independent discretion in fulfilling his or her duties and may not be party to a voting agreement with respect to his or her vote as a director. A violation of these requirements is deemed a breach of the director's duty of loyalty.

The duty of care requires an office holder to act with a level of care that a reasonable office holder in the same position would employ under the same circumstances. This includes the duty to use reasonable means to obtain information regarding the advisability of a given action submitted for his or her approval or performed by virtue of his or her position and all other relevant information material to these actions.

Since the effectiveness of Amendment 20, all arrangements as to compensation of office holders should follow the process described above under "*Compensation Committee.*"

The Israel Companies Law requires that an office holder promptly disclose any personal interest that he or she may have and all related material information known to him or her, in connection with any existing or proposed transaction by the company. "Personal interest," as defined by the Companies Law, includes a personal interest of any person in an act or transaction of the company, including a personal interest of his relative or of a corporation in which that person or a relative of that person is a 5% or greater shareholder, a holder of 5% or more of the voting rights, a director or general manager, or in which he or she has the right to appoint at least one director or the general manager, and includes shares for which the person has the right to vote pursuant to a power-of-attorney. "Personal interest" does not apply to a personal interest stemming merely from holding shares in the company.

The office holder must make the disclosure of his personal interest no later than the first meeting of the company's board of directors that discusses the particular transaction. This duty does not apply to the personal interest of a relative of the office holder in a transaction unless it is an "extraordinary transaction." An "extraordinary transaction" is defined as a transaction not in the ordinary course of business, a transaction that is not on market terms, or a transaction that is likely to have a material impact on the company's profitability, assets or liabilities, and a "relative" as a spouse, sibling, parent, grandparent or descendant, and the sibling, parent or descendant of a spouse, as well as the spouse of any of the foregoing.

In the case of a transaction that is not an extraordinary transaction and that does not relate to compensation or terms of employment, after the office holder complies with the above disclosure requirement, only Board approval is required unless the Articles of Association of the company provide otherwise. Our Amended and Restated Articles of Association do not provide otherwise. Such approval must determine that the transaction is not adverse to the company's interest. If the transaction is an extraordinary transaction, then in addition to any approval required by the Articles of Association, it also must be approved by the audit committee and by the Board and, under specified circumstances, by a meeting of the shareholders. An office holder who has a personal interest in a matter that is considered at a meeting of the Board of Directors or the audit committee generally may not be present at this meeting or vote on this matter unless a majority of the board of directors or the audit committee has a personal interest in the matter, or if such person is invited by the Chairman of the Board of Directors or audit committee, as applicable, to present the matter being considered. If a majority of the board of directors or the audit committee has a personal interest in the transaction, shareholder approval also would be required.

The Israel Companies Law applies the same disclosure requirements set forth above to a controlling shareholder of a public company, which includes a shareholder that holds 25% or more of the voting rights if no other shareholder owns more than 50% of the voting rights in the company. Extraordinary transactions, including a private placement with a controlling shareholder or in which a controlling shareholder has a personal interest (including for the provision of services to the company through a company controlled by a controlling shareholder, but not including transactions covering the terms of compensation of a controlling shareholder who is an office holder), require the approval of the audit committee, the Board of Directors and the shareholders of the company. Extraordinary transactions covering the terms of compensation of a controlling shareholder who is an office holder, require the approval of the compensation committee, the Board of Directors and the shareholders of the company. The shareholder approval must either include a majority of the non-controlling and disinterested shareholders who are present, in person or by proxy, at the meeting or, alternatively, the total shareholdings of the non-controlling and disinterested shareholders who vote against the transaction must not represent more than two percent of the voting rights in the company. Generally, the approval of such a transaction may not extend for more than three years, except that in the case of an extraordinary transaction with a controlling shareholder or in which a controlling shareholder has a personal interest that does not concern terms of compensation for service as an office holder, or as a service provider to the company, the transaction may be approved for a longer period if the audit committee determines that the approval of the transaction for a period longer than three years is reasonable under the circumstances.

Under the Israel Companies Law, a shareholder has a duty to act in good faith towards the company and other shareholders and refrain from abusing his or her power in the company, including, among other things, in respect to his or her voting at the general meeting of shareholders on the following matters:

- any amendment to the Articles of Association;
- an increase of the company's authorized share capital;
- a merger; or
- approval of interested party transactions that require shareholder approval.

In addition, any controlling shareholder, any shareholder who can determine the outcome of a shareholder vote and any shareholder who, under the company's Articles of Association, can appoint or prevent the appointment of an office holder, are under a duty to act with fairness towards the company. The Israel Companies Law provides that a breach of the duty of fairness will be governed by the laws governing breach of contract. The Israel Companies Law does not describe the substance of this duty.

Insurance, Indemnification and Exculpation of Directors and Officers; Limitations on Liability

The Israel Companies Law permits a company to insure an office holder in respect of liabilities incurred by him or her as a result of the breach of his or her duty of care to the company or to another person, or as a result of the breach of his or her duty of loyalty to the company, to the extent that he or she acted in good faith and had reasonable cause to believe that the act would not prejudice the company. A company can also insure an office holder for monetary liabilities as a result of an act or omission that he or she committed in connection with his or her serving as an office holder. Moreover, a company can indemnify an office holder for (a) any monetary liability imposed upon such an office holder for the benefit of a third party pursuant to a court judgment, including a settlement or an arbitrator's decision, confirmed by a court, (b) reasonable legal costs, including attorney's fees, expended by an office holder as a result of an investigation or proceeding instituted against the office holder by a competent authority, provided that such investigation or proceeding concludes without the filing of an indictment against the office holder and either i) no financial liability was imposed on the office holder in lieu of criminal proceedings or ii) financial liability was imposed on the office holder in lieu of criminal proceedings but the alleged criminal offense does not require proof of criminal intent, (c) legal expenses (including attorneys' fees) incurred by an office holder in an administrative enforcement proceeding and any compensation payable to injured parties for damages suffered by them as determined in the proceeding (up to a maximum of 20% of the fine imposed on the violating party) and (d) reasonable litigation expenses, including legal fees, actually incurred by such an office holder or imposed upon the office holder by a court order, in a proceeding brought against the office holder by or on behalf of the company or by others, or in a criminal action in which he was acquitted, or in a criminal action which does not require proof of criminal intent in which he was convicted. The Companies Law further provides that the indemnification provision in a company's articles of association (i) may be an obligation to indemnify in advance, provided that, other than litigation expenses, it is limited to events the board of directors can foresee in light of the company's actual activities when providing the obligation

and that it is limited to a sum or standards the board of directors determines is reasonable in the circumstances, and (ii) may permit the company to indemnify an officer or a director after the fact.

Furthermore, a company can, with one limited exception, exculpate an office holder in advance, in whole or in part, from liability for damages sustained by a breach of duty of care to the company.

All of these provisions are specifically limited in their scope by the Companies Law, which provides that a company may not indemnify or exculpate an officer or director nor enter into an insurance contract that would provide coverage for any monetary liability incurred as a result of (i) a breach by the officer or director of the duty of loyalty, unless the officer or director acted in good faith and had a reasonable basis to believe that the act would not prejudice the company, in which case the company is permitted to indemnify and provide insurance to but not to exculpate; (ii) an intentional or reckless breach by the officer or director of the duty of care, other than if solely done in negligence; (iii) any act or omission done with the intent to derive an illegal personal benefit; or (iv) any fine levied or forfeit against the director or officer.

Our Amended and Restated Articles of Association allow us to insure, exculpate and indemnify office holders to the fullest extent permitted by law provided such insurance, exculpation or indemnification is approved in accordance with the Israel Companies Law. We have acquired directors' and officers' liability insurance covering the officers and directors of Commtouch and its subsidiary for certain claims. At the annual meeting of shareholders held on November 18, 2002, the shareholders approved a form of indemnification, exculpation and insurance agreement that is applicable to all our directors. The form of this agreement, as well as related provisions in our Amended and Restated Articles of Association, were last amended at the annual meeting of shareholders held on December 15, 2011.

Compensation of Directors and Executive Officers

Under Amendment 20, the directors of Commtouch can be remunerated by Commtouch for their services as directors to the extent such remuneration is in accordance with the compensation policy to be adopted by the Company after approval by Commtouch's compensation committee, Board of Directors and shareholders.

The cash compensation paid to directors in 2012 (other than the CEO and Chairman) is as follows:

a. NIS 31,700 base annually per director, as linked to the applicable Israeli consumer price index, payable in four equal installments at the beginning of each calendar quarter; and
b. NIS 1,590 per director per in-person Board or committee meeting, or NIS954 (60% of NIS 1590) in case of telephonic participation at such meeting, payable at the beginning of each calendar quarter following the quarter during which a Board member participated in a meeting. No separate per meeting compensation was paid for committee meetings that were held on the same day immediately prior or subsequent to a Board meeting. In that event, a Board and committee meeting would be considered one meeting for purposes of compensation.
c. For non-Israeli based directors, the amounts set forth will be paid in United States dollars, according to the representative rate of exchange published by the Bank of Israel on the date of payment.

Directors also are reimbursed for their expenses for each Board of Directors meeting attended. See in this item 6, "Amended and Restated 1999 Non-employee Directors Stock Option Plan" for a discussion of director compensation in the form of option grants.

During 2012, options to purchase 166,669 Ordinary Shares were granted to directors and executive officers under the Company's stock option plans at a weighted average exercise price of $3.17 per share. The aggregate direct remuneration paid by Commtouch to all directors and executive officers (11 persons) in 2012 was approximately $971,000. During the same period Commtouch accrued or set aside approximately $53,000 for the same group to provide pension, retirement or similar benefits. As of March 1, 2013, directors and executive officers of Commtouch (9 persons) held an aggregate of 2,058,550 stock options to purchase a like number of Ordinary Shares, with 1,007,530 of those options being vested and exercisable within sixty days of said date. Generally, unless exercised previously, options terminate within six years of their issuance.

At the meeting of shareholders in December 2010, shareholders approved the payment to Hila Karah of up to $10,000 annually for the performance of any additional services as a committee member, as agreed upon by Ms. Karah and the

Company on a case by case basis. During 2011, Ms. Karah received a total of $2,500 for her additional services as a director. No compensation was paid for such additional services during 2012.

Options to Purchase Securities from Registrant or Subsidiaries

As of March 1, 2013, options to purchase 5,718,990 Ordinary Shares were outstanding and held by 198 persons made up of then existing employees, consultants, executive officers, non–employee directors and ex-options holders within their post-termination period for exercise under the Company's stock option plans, and there were 776,282 shares available for grant under all plans. Of the number of options outstanding, 2,032,004 were vested and exercisable. Additionally, these outstanding options had exercise prices ranging from $0.93 to $6.60 per share, a weighted average per share exercise price of approximately $3.16 and termination dates ranging from March 14, 2013 to February 13, 2019.

Employee Stock Option Plans

Employees, including executive officers and other management employees, participate in the Company's employee option plans. The Commtouch Software Ltd. 2006 U.S. Stock Option Plan, primarily covering option grants to employees and consultants based in the United States, was adopted on December 15, 2006 and has a term of ten years. The Commtouch Software Ltd. Amended and Restated Israeli Share Options Plan, primarily covering option grants to employees, consultants and directors based in Israel, was adopted on June 22, 2003 and has a term of ten years. While Israeli based directors receive their grants under the Israeli plan, the principal terms of their grants are identical to those of non-Israeli based directors receiving their grants under the non-employee director plan (discussed below).

All employee stock option plans are administered by the Compensation Committee. Subject to the provisions of the employee stock plans and applicable law, the Compensation Committee has the authority to determine, among other things, to whom options may be granted; the number of Ordinary Shares to which an option may relate; the exercise price for each share; the vesting period of the option and the terms, conditions and restrictions thereof, including accelerated vesting on change of control provisions; to amend provisions relating to such plans; and to make all other determinations deemed necessary or advisable for the administration of such plans.

Amended and Restated 1999 Non–Employee Directors Stock Option Plan

New non-employee directors are currently entitled to an initial grant of 50,000 options pursuant to the Amended and Restated 1999 Non-Employee Directors Stock Option Plan, or the Non-Employee Directors Plan. Non-employee directors who are re-elected at the annual meeting of shareholders are entitled to additional grants of 16,667 options, though at the annual meeting held October 26, 2009 shareholders approved a one-time increase in the grants to re-elected directors to 30,000 options.

The Non–Employee Directors Plan was extended by an additional ten years at the annual meeting of shareholders held on December 15, 2008. Under this plan, each option becomes exercisable at a rate of 1/16th of the option shares every three months, and has an exercise price equal to the fair market value of our Ordinary Shares on the grant date of such option. Options granted through 2004 had a maximum term of ten years, but would terminate earlier if the option holder ceased to be a member of the Board of Directors. Options granted to directors during 2005 - 2012 generally have a maximum term of six years. At the annual meeting of shareholders of December 30, 2005, shareholders approved an amendment to the Non-Employee Directors Plan to allow for the acceleration of unvested options for any director who has served the Company for at least three years, unless the director resigned voluntarily or was removed from the Board of Directors due to a failure to perform any of his/her duties to the Company.

Employees

See Item 4. "Information on the Company—Employees".

Item 7. Major Shareholders and Related Party Transactions.

The following table presents information with respect to beneficial ownership of our Ordinary Shares as of March 1, 2013, including:

- each person or entity known to Commtouch to own beneficially five percent or more of Commtouch's Ordinary Shares, and
- all executive officers and directors as a group.

Beneficial ownership is determined in accordance with the rules of the SEC and includes voting or investment power, with respect to shares. To our knowledge, except under applicable community property laws or as otherwise indicated, the persons named in the table have sole voting and sole investment control and rights to receive economic benefits with respect to all shares beneficially owned. The applicable percentage of ownership for each shareholder is based on 26,061,383 Ordinary Shares outstanding as of March 1, 2013. Ordinary Shares issuable upon exercise of options, which are exercisable on or within sixty days of March 1, 2013, are deemed outstanding for the purpose of computing the percentage ownership of the person holding those options for all directors and executive officers as a group, but are not deemed outstanding for computing the percentage ownership of any other person. Major shareholders in the Company have the same voting rights as all other shareholders.

MAJOR SHAREHOLDERS OF ORDINARY SHARES	Amount Owned	Percent of Class
Aviv Raiz*(1)	5,561,068	21.3%
Catalyst Private Equity Partners II LP*(2)	1,372,555	5.2%
All directors and executive officers as a group [at 3/1/13] (9 persons)(3)	7,851,195	29.3%

*This shareholder of record resides in Israel. With respect to Catalyst Private Equity Partners II LP, the former Chairman and Managing Partner of this limited partnership, Mr. Yair Shamir, a former director of the Company, resides in Israel.
(1)Includes 75,199 options, exercisable into a like number of Ordinary Shares.
(2)Includes 108,532 options exercisable into a like number of Ordinary Shares.
(3)Includes 769,198 options exercisable into a like number of Ordinary Shares.

Based on a review of the information provided to us by third parties, including our transfer agent, as of March 1, 2013, there were 53 holders of record of our Ordinary Shares. One of such holders is the nominee company known as CEDE & Co., which held 21,592,221 Ordinary Shares on behalf of approximately 81 brokers and banks, or approximately 83% of the aggregate 26,061,383 Ordinary Shares outstanding as of such date. Out of the 21,592,221 Ordinary Shares held through CEDE, approximately 15.4 million are managed by Broadridge Financial Solutions, Inc. on behalf of certain banks and brokers, and Broadridge recently provided to us reports on the geographical location of shareholders holding through such banks and brokers. According to these reports, plus our transfer agent reports, we were able to identify at least 13.7 million Ordinary Shares held by Israeli shareholders, approximately 5.3 million shares held US based shareholders and 3.4 million held by non-Israeli and non-U.S. shareholders.

Significant Changes in Percentage Ownership of Major Shareholders During the Past Three Years

None.

Interest of Management and their Family Members in Certain Transactions

There were no related party transactions, as such term if defined in Item 7.B to Form 20-F, during 2012 or through the date of filing of this Annual Report.

Item 8. Financial Information.

See Item 18: Financial Statements. If the Company decides to distribute a cash dividend out of income that has been tax exempt due to an "approved enterprise" status under the Law for the Encouragement of Capital Investments, 5719-1959, the amount of cash dividend will be subject to corporate tax at the rate then in effect under Israeli law. The Company has never declared or paid cash dividends on its Ordinary Shares. However, the Company has not adopted a policy not to pay cash dividends and therefore may declare a dividend in the future. The Company's current plans are to retain future earnings primarily to finance the development of its business and for other corporate purposes.

Legal Proceedings

In December 2012, our U.S. subsidiary filed a lawsuit in the Superior Court of the State of California against one of its largest customers, Watchguard Technologies, Inc. The lawsuit includes a claim for breach of contract. In mid-April 2013, Watchguard filed its formal answer and a cross-complaint to Commtouch's complaint. Commtouch's lawsuit alleges damages in excess of $7 million, while WatchGuard's cross-complaint does not set forth a fixed amount that it is seeking. It is expected that the discovery phase of the litigation will commence in the near future.

Our new subsidiary company, eleven, is currently involved in three lawsuits: i) the first relates to a claim by a former employee regarding payment of a commission alleged to be in the amount of approximately EURO 139,000; ii) the second relates to a claim by a hardware vendor in the amount of approximately EURO 90,000; and iii) the final claim was brought by eleven against Boxsentry, a customer, for failure to pay fees in the amount of approximately EURO 840,000.

Other than the above, we are not a direct party to any litigation, and we are not aware of any threatened litigation which, in the aggregate, would be material to the business of the Company. As noted under Item 3. Key Information – Risk Factors, one customer has made an indemnification demand on us during the past year as a result of patent infringement actions brought against that customer and other defendants.

Except as otherwise disclosed in this Annual Report, there has been no material change in our financial position since December 31, 2012.

Item 9. The Offer and Listing.

The Company's Ordinary Shares have been traded publicly on NASDAQ as follows:

a. From July 13, 1999 through June 29, 2004, under the symbol "CTCH" (up to June 7, 2002 on the National Market, and subsequently on the Small Cap Market, which during 2005 was renamed the "Capital Market");

b. From June 30, 2004 through June 26, 2005, under the symbol "CTCHC";

c. From June 27, 2005 through January 1, 2008, under the symbol "CTCH";

d. From January 2, 2008 through January 29, 2008, under the symbol "CTCHD"; and

e. From January 30, 2008, under the symbol CTCH.

Since December 16, 2009, the Company's Ordinary Shares have also been traded on the Tel Aviv Stock Exchange, or "TASE", under the symbol CTCH.

The following table lists the high and low closing sales prices for the Company's Ordinary Shares on the NASDAQ Capital Market for the periods indicated:

	High	Low
2008:	$ 6.22	$ 1.50
2009:	$ 4.30	$ 1.57
2010:	$ 3.90	$ 1.35
2011:	$ 3.98	$ 2.93
2012:	$ 3.40	$ 2.42
2011:		
First Quarter	$ 3.98	$ 3.23
Second Quarter	$ 3.59	$ 3.20
Third Quarter	$ 3.66	$ 2.95
Fourth Quarter	$ 3.60	$ 2.93
2012:		
First Quarter	$ 3.40	$ 2.90
Second Quarter	$ 3.21	$ 2.42
Third Quarter	$ 3.00	$ 2.48
Fourth Quarter	$ 3.20	$ 2.42
First Quarter 2013	$ 3.87	$ 2.91
Most Recent Six Months:		
October 2012	$ 2.70	$ 2.42
November 2012	$ 3.19	$ 2.44
December 2012	$ 3.20	$ 3.00
January 2013	$ 3.19	$ 2.92
February 2013	$ 3.87	$ 3.04
March 2013	$ 3.50	$ 2.91

The following table lists the high and low closing sales prices for the Company's Ordinary Shares on the TASE for the periods indicated. Share prices on the TASE are quoted in NIS:

	High	Low
2011:		
First Quarter	NIS 14.47	NIS 11.87
Second Quarter	NIS 12.50	NIS 10.97
Third Quarter	NIS 12.81	NIS 10.75
Fourth Quarter	NIS 13.82	NIS 11.48
2012:		
First Quarter	NIS 13.37	NIS 10.83
Second Quarter	NIS 12.76	NIS 9.22
Third Quarter	NIS 11.64	NIS 10.06
Fourth Quarter	NIS 12.34	NIS 9.49
First Quarter 2013	NIS 14.29	NIS 10.62
Most Recent Six Months:		
October 2012	NIS 10.55	NIS 9.49
November 2012	NIS 12.34	NIS 9.88
December 2012	NIS 12.07	NIS 11.57
January 2013	NIS 12.03	NIS 11.58
February 2013	NIS 14.29	NIS 11.27
March 2013	NIS 13.21	NIS 10.62

Item 10. Additional Information.

We are registered under the Israel Companies Law as a public company with registration number 52-004418-1. The objective stated in our memorandum of association is to engage in any lawful activity.

DESCRIPTION OF SHARES

Set forth below is a summary of the material provisions governing our share capital. This summary is not complete and should be read together with our Memorandum of Association and Amended and Restated Articles of Association, copies of which are filed with this Annual Report or have been filed as exhibits to certain of our prior filings with the SEC.

As of December 31, 2012, our authorized share capital consisted of 55,353,340 Ordinary Shares, NIS 0.15 par value. As of March 1, 2013, there were 26,061,383 Ordinary Shares issued and outstanding.

DESCRIPTION OF ORDINARY SHARES

All issued and outstanding Ordinary Shares of Commtouch are duly authorized and validly issued, fully paid and non-assessable.

The Ordinary Shares do not have preemptive rights. Our Memorandum of Association, Amended and Restated Articles of Association and the laws of the State of Israel do not restrict in any way the ownership or voting of Ordinary Shares by non–residents of Israel, except with respect to subjects of countries which are in a state of war with Israel.

DIVIDEND AND LIQUIDATION RIGHTS

The Ordinary Shares are entitled to their full proportion of any cash or share dividend declared.

Subject to the rights of the holders of shares with preferential or other special rights that may be authorized, the holders of Ordinary Shares are entitled to receive dividends in proportion to the sums paid up or credited as paid up on account of the nominal value of their respective holdings of the shares in respect of which the dividend is being paid (without taking into account the premium paid up on the shares) out of assets legally available therefor and, in the event of our winding up, to share ratably in all assets remaining after payment of liabilities in proportion to the nominal value of their respective holdings of the shares in respect of which such distribution is being made, subject to applicable law. Declaration of a dividend requires Board of Directors approval.

Under current Israeli regulations, any dividends or other distributions paid in respect of Ordinary Shares purchased by non-residents of Israel with certain non–Israeli currencies (including U.S. dollars) will be freely repatriated in such non-Israeli currencies at the rate of exchange prevailing at the time of conversion, provided that Israeli income tax has been paid on, or withheld from, such payments.

MODIFICATION OF CLASS RIGHTS

If at any time the share capital is divided into different classes of shares, then, unless the conditions of allotment of such class provide otherwise, the rights, additional rights, advantages, restrictions and conditions attached or not attached to any class, at any given time, may be modified, enhanced, added or abrogated by resolution at a meeting of the holders of the shares of such class.

Pursuant to Israel’s securities laws, a company registering its shares for trade on the Tel Aviv Stock Exchange may not have more than one class of shares for a period of one year following registration, after which it is permitted to issue preferred shares, if the preference of those shares is limited to a preference in the distribution of dividends and these preferred shares have no voting rights.

SPECIAL PROVISIONS IN AMENDED AND RESTATED ARTICLES OF ASSOCIATION RELATING TO DIRECTORS

The discussion regarding approval of director compensation and transactions with the Company under "Item 6. Directors, Senior Management and Employees - Approval of Certain Transactions; Obligations of Directors, Officers and Shareholders" is incorporated herein by reference.

VOTING, SHAREHOLDER MEETINGS AND RESOLUTIONS

Holders of Ordinary Shares have one vote for each share held on all matters submitted to a vote of shareholders.

An annual general meeting must be held once every calendar year at such time (not more than 15 months after the last preceding annual general meeting) and at such place, either within or outside the State of Israel, as may be determined by the Board of Directors. The quorum required for a general meeting of shareholders consists of at least two shareholders present in person or by proxy and holding at least one-third of the voting rights of the issued share capital. A meeting adjourned for lack of a quorum may be adjourned to the same day in the next week at the same time and place, or to such time and place as the Board of Directors may determine in a notice to shareholders. At such reconvened meeting any two shareholders entitled to vote and present in person or by proxy will constitute a quorum. Rule 5620(c) to Nasdaq Listing Rules requires that an issuer listed on Nasdaq should have a quorum requirement that in no case be less than 33 1/3% of the outstanding shares of the company's common voting stock. However, as mentioned above, our articles of association, consistent with the Companies Law, provides for a lower quorum requirement at an adjourned meeting.

Generally, shareholder resolutions will be deemed adopted if approved by the holders of a majority of the voting power represented at the meeting, in person or by proxy, and voting thereon. For certain matters as described under the Israel Companies law, there is a requirement that the majority include the affirmative vote of at least a majority of the votes cast by shareholders who are not controlling shareholders of the Company or interested parties in the matter to be voted upon (or their representatives) or, alternatively, the total shareholdings of the votes cast against the proposal (other than by the Company's controlling shareholders or interested parties in the matter to be voted upon) must not represent more than two percent of the voting rights in the Company.

ANTI–TAKEOVER PROVISIONS UNDER ISRAELI LAW

Under the Companies Law, a merger is generally required to be approved by the shareholders and board of directors of each of the merging companies. If the share capital of the company that will not be the surviving company is divided into different classes of shares, the approval of each class is also required. In addition, a merger can be completed only after 30 days have passed from the shareholders' approval of each of the merging companies, all approvals have been submitted to the Israeli Registrar of Companies and at least fifty days have passed from the time that a proposal for approval of the merger was filed with the Registrar.

The Companies Law provides that an acquisition of shares in a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would hold 25% or more of the voting rights in the company, unless there is already another 25% shareholder of the company. Similarly, the Companies Law provides that an acquisition of shares in a public company must be made by means of tender offer if as a result of the acquisition the purchaser would hold more than 45% of the voting rights in the company, unless someone else already holds 45% of the voting power of the company.

Finally, Israeli tax law treats specified acquisitions, including a stock–for–stock swap between an Israeli company and a foreign company, less favorably than does U.S. tax law. For example, Israeli tax law may subject a shareholder who exchanges his Ordinary Shares for shares in a foreign corporation to taxation before it would become taxable in the United States, even though the investment has not become liquid, although in the case of shares of a foreign corporation that are traded on a stock exchange, the tax may be postponed subject to certain conditions.

TRANSFER OF SHARES AND NOTICES

Fully paid Ordinary Shares that are issued and not subject to any legal restrictions on transference may be transferred freely. Each shareholder of record is entitled to receive at least twenty-one days' prior notice (and for certain matters,

thirty-five days' prior notice) before the date of a shareholder meeting and at least five days' notice before the record date for the meeting. For purposes of determining the shareholders entitled to notice of and to vote at such meeting, the Board of Directors may fix a record date not exceeding 40 days prior to the date of any shareholder meeting.

CHANGES IN OUR CAPITAL

Changes in our capital are subject to the approval of the shareholders by a majority of the votes of shareholders present by person or by proxy and voting at the shareholders meeting.

ACCESS TO INFORMATION

We file reports with the Israeli Registrar of Companies regarding our registered address, our registered capital, our shareholders of record and the number of shares held by each, the identity of the directors and details regarding security interests on our assets. In addition, Commtouch must file with the Israeli Registrar of Companies its Amended and Restated Articles of Association and any further amendments thereto. The information filed with the Registrar of Companies is available to the public. In addition to the information available to the public, our shareholders are entitled, upon request, to review and receive copies of all minutes of meetings of our shareholders.

We are subject to certain of the information reporting requirements of the Exchange Act. As a "foreign private issuer," we are exempt from the rules and regulations under the Exchange Act prescribing the furnishing and content of proxy statements, and our officers, directors and principal shareholders are exempt from the reporting and "short-swing" profit recovery provisions contained in Section 16 of the Exchange Act, with respect to their purchase and sale of our Ordinary Shares. In addition, we are not required to file reports and financial statements with the SEC as frequently or as promptly as U.S. companies whose securities are registered under the Exchange Act. However, we file with the SEC an Annual Report on Form 20-F containing financial statements audited by an independent registered public accounting firm. We also furnish quarterly reports on Form 6-K containing unaudited financial information after the end of each quarter and other reports on Form 6-K from time to time. We post our Annual Report on Form 20-F on our Website (www.commtouch.com) promptly following the filing of our Annual Report with the Securities and Exchange Commission. The information on our website is not incorporated by reference into this Annual Report.

This Annual Report and other information filed or to be filed by us can be inspected and copied at the public reference facilities maintained by the SEC at:

100 F Street, NE
Public Reference Room
Washington, D.C. 20549

The SEC maintains a Web site at www.sec.gov that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system.

In addition, since we are also listed on the Tel Aviv Stock Exchange we submit copies of all our filings with the Securities and Exchange Commission to the Israeli Securities Authority and the Tel Aviv Stock Exchange. Such copies can be retrieved electronically through the Tel Aviv Stock Exchange's internet messaging system (www.maya.tase.co.il) and through the MAGNA distribution site of the Israeli Securities Authority (www.magna.isa.gov.il).

MATERIAL CONTRACTS DURING PAST TWO YEARS

Company Acquisition of Frisk Software International's Antivirus Business (hereinafter the "division")

In July 2012, Commtouch and Frisk, entered into a definitive agreement under which Commtouch agreed to acquire the division, including:

i. Antivirus products, including its F-PROT line of products, which are aimed at protecting customers against spyware, Trojan downloaders and other such Internet related threats;

ii. certain contracts with OEM licensees pursuant to which such licensees are authorized to integrate the FRISK antivirus engine API/SDK into their solutions and to sell and support such integrated solutions;

iii. certain contracts with distributors and resellers pursuant to which such entities are authorized to sell the F-PROT products;

iv. all such products' intellectual property, including all interests in relevant brand names and all associated trademarks, trade names and related property;

v. all accounts receivable relating to this division; and

vi. certain furniture, fixtures, equipment, office equipment, supplies, computers and other tangible personal property connected with the division.

In consideration for the sale of this division, Commtouch agreed to pay i) in cash, the sum of $2.2 million, $1 million of which was placed in escrow for payment in one installment on the one year anniversary of closing, provided those funds are not needed to satisfy certain obligations of the division relating to the pre-closing period, and ii) in equity, 750,000 restricted Ordinary Shares in Commtouch, vesting in annual installments over four years commencing on the first anniversary of the closing date. Additionally, from the closing and through March 31, 2015, Commtouch is required to make periodic earnout payments to the sellers equal to 5% of the combined revenue generated by all Commtouch antivirus solutions.

The closing of the transaction occurred on October 1, 2012, and Commtouch, through a new Icelandic company known as Commtouch Iceland hf, added approximately 37 new employees at that time.

Company Acquisition of eleven GmbH

On November 16, 2012, Commtouch and eleven simultaneously signed and closed a share purchase agreement under which we acquired eleven, including:

i. all outstanding shares of eleven from its current shareholders;

ii. eleven's products and services, including its eXpurgate line of products, which are aimed at protecting customers against email-borne spam, viruses and other such Internet related threats;

iii. all contracts with OEM licensees pursuant to which such licensees are authorized to integrate the eleven API/SDK into their solutions and to sell and support such integrated solutions;

iv. all contracts with distributors and resellers pursuant to which such entities are authorized to sell the eleven products and services;

v. all direct contracts with enterprises, businesses, and ISPs pursuant to which eleven provides direct service through a hosted managed service offering or on-premise managed platform;

vi. all eleven products' intellectual property, including all interests in relevant brand names and all associated trademarks, trade names and related property; and

vii. all assets and liabilities of eleven, including all fixed assets, such as data center servers, computer equipment, furniture, fixtures, office equipment, supplies, and other tangible personal property connected with eleven.

In consideration for the sale of eleven, at the closing Commtouch paid:

i. in cash, the sum of Euro 9.05 million (approximately $11.53 million based on the exchange rate on the date of acquisition), including €1.84 million ($2.34 million) cash which will stay in the business for a net purchase price of €7.21 million ($9.19 million); €0.82 million ($1.05 million) of the cash price will be placed in escrow, for release to the sellers in one installment on the one year anniversary of the closing of the transaction, provided those funds are not needed to satisfy certain obligations of eleven relating to the pre-closing period;

ii. in equity, 806,750 restricted Ordinary Shares in Commtouch, with a value of approximately $2.10 million based on an averaging of Commtouch's Ordinary Share price on the day of closing, vesting in equal annual installments over a 2 year vesting period commencing on the first anniversary of the closing date; and

iii. additionally, from the closing and through December, 2015, Commtouch shall make periodic earnout payments to the sellers calculated at between 3% - 12% of certain revenues generated by eleven's platform, products, and services.

c. At the closing, 60 new employees joined the Commtouch organization by virtue of the acquisition of eleven.

Company Credit Lines

During 2012, we made significant investments (from our cash reserves) in the above described acquisitions of eleven and Frisk. Due in part to these investments, at about the time of the filing of this Annual Report, a credit line had been secured from an Israeli bank, and we were in the process of closing on another credit line with a second Israeli bank. Together, both credit lines total a sum of up to $5,000,000. These credit lines are being put in place in order to ensure sufficient cash is available to fund the strategic growth investments of the Company.

In relation to these credit lines, the Company has agreed to grant security interests generally over all Company assets, and to refrain from encumbering its assets in favor of any other third parties. The Company has already drawn on one of the credit lines in the amount of $1.5 million.

EXCHANGE CONTROLS

Non-residents of Israel who own our Ordinary Shares may freely convert all amounts received in Israeli currency in respect of such Ordinary Shares, whether as a dividend, liquidation distribution or as proceeds from the sale of our Ordinary Shares, into non-Israeli currencies at the rate of exchange prevailing at the time of conversion (provided in each case that the applicable Israeli income tax, if any, is paid or withheld).

Until May 1998, Israel imposed extensive restrictions on transactions in foreign currency. These restrictions were largely lifted in May 1998. Since January 1, 2003, all exchange control restrictions have been eliminated although there are still reporting requirements for certain foreign currency transactions. Legislation remains in effect, however, pursuant to which currency controls can be imposed by administrative action at any time.

The State of Israel does not restrict in any way the ownership or voting of our Ordinary Shares by non-residents of Israel, except with respect to subjects of countries that are in a state of war with Israel.

ISRAELI TAXATION

The following is a summary of the principal tax laws applicable to companies in Israel, including special reference to their effect on us, and Israeli government programs benefiting us. This section also contains a discussion of the material Israeli tax consequences to you if you acquire Ordinary Shares of our company. This summary does not discuss all the acts of Israeli tax law that may be relevant to you in light of your personal investment circumstances or if you are subject to special treatment under Israeli law. To the extent that the discussion is based on new tax legislation which has not been subject to judicial or administrative interpretation, we cannot assure you that the views expressed in this discussion will be accepted by the tax authorities. The discussion should not be understood as legal or professional tax advice and is not exhaustive of all possible tax considerations.

General Corporate Tax Structure

Israeli companies were generally subject to corporate tax at the rate of 24% of their taxable income in 2011. Corporate tax rates applicable for 2008, 2009 and 2010 were 27%, 26% and 25%, respectively.

On December 5, 2011, the Israeli Parliament (the Knesset) passed the Law for Tax Burden Reform (Legislative Amendments), 2011 which, among others, effective from 2012 cancels the scheduled progressive reduction in the corporate tax rate, and increases the corporate tax rate to 25% in 2012 and subsequent years.

Tax Benefits under the Law for the Encouragement of Industry (Taxes), 1969

The Law for the Encouragement of Industry (Taxes), 1969, generally referred to as the Industry Encouragement Law, provides several tax benefits for industrial companies. An industrial company is defined as a company resident in

Israel, at least 90% of the income of which in a given tax year exclusive of income from specified government loans, capital gains, interest and dividends, is derived from an industrial enterprise owned by it. An industrial enterprise is defined as an enterprise whose major activity in a given tax year is industrial production activity.

Under the Industry Encouragement Law, industrial companies are entitled to a number of corporate tax benefits, including:

- deduction of purchase of know-how and patents and/or right to use a patent over an eight-year period;
- the right to elect, under specified conditions, to file a consolidated tax return with additional related Israeli industrial companies and an industrial holding company;
- accelerated depreciation rates on equipment and buildings.
- Expenses related to a public offering on TA stock exchange and as of 1.1.2003 on recognized stock markets outside of Israel, are deductible in equal amounts over three years.

Under some tax laws and regulations, an industrial enterprise may be eligible for special depreciation rates for machinery, equipment and buildings. These rates differ based on various factors, including the date the operations begin and the number of work shifts. An industrial company owning an approved enterprise may choose between these special depreciation rates and the depreciation rates available to the approved enterprise.

Eligibility for benefits under the Industry Encouragement Law is not subject to receipt of prior approval from any governmental authority.

We believe that we currently qualify as an industrial company within the definition of the Industry Encouragement Law. We cannot assure you that the Israeli tax authorities will agree that we qualify, or, if we qualify, that we will continue to qualify as an industrial company or that the benefits described above will be available to us in the future.

Capital Gains Tax on Sales of Our Ordinary Shares

Israeli law generally imposes a capital gains tax on the sale of any capital assets by residents of Israel, as defined for Israeli tax purposes, and on the sale of assets located in Israel, including shares in Israeli companies, by both residents and non-residents of Israel, unless a specific exemption is available or unless a tax treaty between Israel and the shareholder's country of residence provides otherwise. The law distinguishes between real gain and inflationary surplus. The inflationary surplus is a portion of the total capital gain which is equivalent to the increase of the relevant asset's purchase price which is attributable to the increase in the Israeli consumer price index or, in certain circumstances, a foreign currency exchange rate, between the date of purchase and the date of sale. The real gain is the excess of the total capital gain over the inflationary surplus.

As of January 1, 2006, the tax rate applicable to capital gains derived from the sale of shares, whether listed on a stock market or not, is 20% for Israeli individuals, unless such shareholder claims a deduction for financing expenses in connection with such shares, in which case the gain will generally be taxed at a rate of 25%. Additionally, if such shareholder is considered a "material shareholder" at any time during the 12-month period preceding such sale, i.e., such shareholder holds directly or indirectly, including with others, at least 10% of any means of control in the company, the tax rate shall be 25%. Israeli companies are subject to the Corporate Tax rate on capital gains derived from the sale of shares, unless such companies were not subject to the Adjustments Law (or certain regulations) at the time of publication of the aforementioned amendment to the Tax Ordinance that came into effect on January 1, 2006, in which case the applicable tax rate is 25%. However, the foregoing tax rates do not apply to: (i) dealers in securities; and (ii) shareholders who acquired their shares prior to an initial public offering (that may be subject to a different tax arrangement).

Non-Israeli residents are exempt from Israeli capital gains tax on any gains derived from the sale of shares of Israeli companies publicly traded on a recognized stock exchange or regulated market outside of Israel, provided however that such capital gains are not derived from a permanent establishment in Israel, such shareholders are not subject to the Adjustments Law, and such shareholders did not acquire their shares prior to an initial public offering. However, non-Israeli corporations will not be entitled to such exemption if an Israeli resident (i) has a controlling interest of 25% or more in such non-Israeli corporation, or (ii) is the beneficiary or is entitled to 25% or more of the revenues or profits of such non-Israeli corporation, whether directly or indirectly.

In some instances where our shareholders may be liable to Israeli tax on the sale of their Ordinary Shares, the payment of the consideration may be subject to the withholding of Israeli tax at the source.

Pursuant to the Convention Between the government of the United States of America and the government of Israel with Respect to Taxes on Income, as amended (the "U.S.-Israel Tax Treaty"), the sale, exchange or disposition of Ordinary Shares by a person who (i) holds our Ordinary Shares as a capital asset, (ii) qualifies as a resident of the United States within the meaning of the U.S.-Israel Tax Treaty and (iii) is entitled to claim the benefits afforded to such person by the U.S.-Israel Tax Treaty, generally, will not be subject to the Israeli capital gains tax. Such exemption will not apply if (i) such Treaty U.S. Resident holds, directly or indirectly, shares representing 10% or more of our voting power during any part of the 12-month period preceding such sale, exchange or disposition, subject to certain conditions, or (ii) the capital gains from such sale, exchange or disposition can be allocated to a permanent establishment in Israel. In such case, the sale, exchange or disposition of Ordinary Shares would be subject to Israeli tax, to the extent applicable; however, under the U.S.-Israel Tax Treaty, such Treaty U.S. Resident would be permitted to claim a credit for such taxes against the U.S. federal income tax imposed with respect to such sale, exchange or disposition, subject to the limitations in U.S. laws applicable to foreign tax credits. The U.S.-Israel Tax Treaty does not relate to U.S. state or local taxes.

Taxation of Non-Resident Holders of Shares

Non-residents of Israel are subject to income tax on income accrued or derived from sources in Israel. Such sources of income include passive income such as dividends, royalties and interest, as well as non-passive income from services rendered in Israel. On distributions of dividends other than bonus shares, or stock dividends, income tax is withheld at the source at the following rates: for dividends distributed on or after January 1, 2006 - 20%, or 25% for a shareholder that is considered a "material shareholder" at any time during the 12-month period preceding such distribution, unless a different rate is provided in a treaty between Israel and the shareholder's country of residence. Under the U.S.-Israel Tax Treaty, the maximum tax on dividends paid to a holder of our Ordinary Shares who is a Treaty U.S. Resident is 25%. Furthermore, dividends not generated by an Approved Enterprise (or Benefited Enterprise) paid to a U.S. corporation holding at least 10% of our issued voting power during the part of the tax year which precedes the date of payment of the dividend and during the whole of its prior tax year, are generally taxed at a rate of 12.5%.

For information with respect to the applicability of Israeli capital gains taxes on the sale of Ordinary Shares by United States residents, see above "— Capital Gains Tax on Sales of Our Ordinary Shares."

UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

THE FOLLOWING SUMMARY IS INCLUDED HEREIN FOR GENERAL INFORMATION AND IS NOT INTENDED TO BE, AND SHOULD NOT BE CONSIDERED TO BE, LEGAL OR TAX ADVICE. EACH U.S. HOLDER SHOULD CONSULT WITH HIS OR HER OWN TAX ADVISOR AS TO THE PARTICULAR U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE PURCHASE, OWNERSHIP AND SALE OF OUR ORDINARY SHARES, INCLUDING THE EFFECTS OF APPLICABLE STATE, LOCAL, FOREIGN OR OTHER TAX LAWS AND POSSIBLE CHANGES IN THE TAX LAWS.

U.S. Federal Income Taxation

Subject to the limitations described in the next paragraph, the following discussion summarizes the material U.S. federal income tax consequences to a "U.S. Holder" arising from the purchase, ownership and sale of our Ordinary Shares. For this purpose, a "U.S. Holder" is a holder of Ordinary Shares that is: (1) an individual citizen or resident of the United States, including an alien individual who is a lawful permanent resident of the United States or meets the substantial presence residency test under U.S. federal income tax laws; (2) a corporation (or other entity treated as a corporation for U.S. federal income tax purposes) or a partnership (other than a partnership that is not treated as a U.S. person under any applicable U.S. Treasury Regulations) created or organized in or under the laws of the United States or the District of Columbia or any political subdivision thereof; (3) an estate, the income of which is subject to U.S. federal income tax regardless of source; (4) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have authority to control all substantial decisions of the trust; (5) a trust that has a valid election in effect to be treated as a U.S. person to the extent provided in

U.S. Treasury Regulations; or (6) any person otherwise subject to U.S. federal income tax on a net income basis in respect of our Ordinary Shares, if such status as a U.S. Holder is not overridden pursuant to the provisions of an applicable tax treaty.

This summary is for general information purposes only and does not purport to be a comprehensive description of all of the U.S. federal income tax considerations that may be relevant to a decision to purchase or hold our Ordinary Shares. This summary generally considers only U.S. Holders that will own our Ordinary Shares as capital assets. Except to the limited extent discussed below, this summary does not consider the U.S. federal tax consequences to a person that is not a U.S. Holder, nor does it describe the rules applicable to determine a taxpayer's status as a U.S. Holder. This summary is based on the provisions of the Internal Revenue Code of 1986, as amended, or the Code, final, temporary and proposed U.S. Treasury Regulations promulgated thereunder, administrative and judicial interpretations thereof, and the U.S./Israel Income Tax Treaty, all as in effect as of the date hereof and all of which are subject to change, possibly on a retroactive basis, and all of which are open to differing interpretations. Commtouch will not seek a ruling from the U.S. Internal Revenue Service, or the IRS, with regard to the U.S. federal income tax treatment of an investment in our Ordinary Shares by U.S. Holders and, therefore, can provide no assurances that the IRS will agree with the conclusions set forth below.

This discussion does not address all of the aspects of U.S. federal income taxation that may be relevant to a particular shareholder based on such shareholder's particular circumstances and in particular does not discuss any estate, gift, generation-skipping, transfer, state, local or foreign tax considerations. In addition, this discussion does not address the U.S. federal income tax treatment of a U.S. Holder who is: (1) a bank, life insurance company, regulated investment company, or other financial institution or "financial services entity"; (2) a broker or dealer in securities or foreign currency; (3) a person who acquired our Ordinary Shares in connection with employment or other performance of services; (4) a U.S. Holder that is subject to the U.S. alternative minimum tax; (5) a U.S. Holder that holds our Ordinary Shares as a hedge or as part of a hedging, straddle, conversion or constructive sale transaction or other risk-reduction transaction for U.S. federal income tax purposes; (6) a tax-exempt entity; (7) real estate investment trusts; (8) a U.S. Holder that expatriates out of the United States or a former long-term resident of the United States; or (9) a person having a functional currency other than the U.S. dollar. This discussion does not address the U.S. federal income tax treatment of a U.S. Holder that owns, directly or constructively, at any time, Ordinary Shares representing 10% or more of our voting power. Additionally, the U.S. federal income tax treatment of persons who hold Ordinary Shares through a partnership or other pass-through entity are not considered.

You are encouraged to consult your own tax advisor with respect to the specific U.S. federal and state income tax consequences to you of purchasing, holding or disposing of our Ordinary Shares, including the effects of applicable state, local, foreign or other tax laws and possible changes in the tax laws.

Distributions on Ordinary Shares

Subject to the discussion under the heading "Passive Foreign Investment Companies" below, a U.S. Holder will be required to include in gross income as ordinary income the amount of any distribution paid on Ordinary Shares (including the amount of any Israeli tax withheld on the date of the distribution), to the extent that such distribution does not exceed our current and accumulated earnings and profits, as determined for U.S. federal income tax purposes. The amount of a distribution which exceeds our earnings and profits will be treated first as a non-taxable return of capital, reducing the U.S. Holder's tax basis in its Ordinary Shares to the extent thereof, and then capital gain. Corporate holders generally will not be allowed a deduction for dividends received. For non-corporate U.S. Holders, to the extent that their total adjusted income does not exceed applicable thresholds, the maximum federal income tax rate for "qualified dividend income" and long-term capital gains is generally 15%. For those non-corporate U.S. Holders whose total adjusted income exceeds such income thresholds, the maximum federal income tax rate on "qualified dividend income" and long-term capital gains is generally 20%. For this purpose, "qualified dividend income" means, *inter alia*, dividends received from a "qualified foreign corporation." A "qualified foreign corporation" is a corporation that is entitled to the benefits of a comprehensive tax treaty with the United States which includes an exchange of information program. The IRS has stated that the Israel/U.S. Tax Treaty satisfies this requirement and we believe we are eligible for the benefits of that treaty.

In addition, our dividends will be qualified dividend income if our Ordinary Shares are readily tradable on NASDAQ or another established securities market in the United States. Dividends will not qualify for the preferential rate if we

are treated, in the year the dividend is paid or in the prior year, as a passive foreign investment company, or PFIC. A U.S. Holder will not be entitled to the preferential rate: (i) if the U.S. Holder has not held our Ordinary Shares or ADRs for at least 61 days of the 121 day period beginning on the date which is 60 days before the ex-dividend date, or (ii) to the extent the U.S. Holder is under an obligation to make related payments on substantially similar property. Any days during which the U.S. Holder has diminished its risk of loss on our Ordinary Shares are not counted towards meeting the 61-day holding period. Finally, U.S. Holders who elect to treat the dividend income as "investment income" pursuant to Code section 163(d)(4) will not be eligible for the preferential rate of taxation.

The amount of a distribution with respect to our Ordinary Shares will be measured by the amount of the fair market value of any property distributed, and for U.S. federal income tax purposes, the amount of any Israeli taxes withheld therefrom. (See discussion above under "Taxation of Non-Resident Holders of Shares.") Cash distributions paid by us in NIS will be included in the income of U.S. Holders at a U.S. dollar amount based upon the spot rate of exchange in effect on the date the dividend is includible in the income of the U.S. Holder, and U.S. Holders will have a tax basis in such NIS for U.S. federal income tax purposes equal to such U.S. dollar value. If the U.S. Holder subsequently converts the NIS, any subsequent gain or loss in respect of such NIS arising from exchange rate fluctuations will be U.S. source ordinary exchange gain or loss.

Distributions paid by us will generally be foreign source income for U.S. foreign tax credit purposes. Subject to the limitations set forth in the Code, U.S. Holders may elect to claim a foreign tax credit against their U.S. income tax liability for Israeli income tax withheld from distributions received in respect of our Ordinary Shares. In general, these rules limit the amount allowable as a foreign tax credit in any year to the amount of regular U.S. tax for the year attributable to foreign source taxable income. This limitation on the use of foreign tax credits generally will not apply to an electing individual U.S. Holder whose creditable foreign taxes during the year do not exceed $300, or $600 for joint filers, if such individual's gross income for the taxable year from non-U.S. sources consists solely of certain passive income. A U.S. Holder will be denied a foreign tax credit with respect to Israeli income tax withheld from dividends received with respect to our Ordinary Shares if such U.S. Holder has not held our Ordinary Shares for at least 16 days out of the 31-day period beginning on the date that is 15 days before the ex-dividend date or to the extent that such U.S. Holder is under an obligation to make certain related payments with respect to substantially similar or related property. Any day during which a U.S. Holder has substantially diminished his or her risk of loss with respect to our Ordinary Shares will not count toward meeting the 16-day holding period. A U.S. Holder will also be denied a foreign tax credit if the U.S. Holder holds our Ordinary Shares in an arrangement in which the U.S. Holder's reasonably expected economic profit is insubstantial compared to the foreign taxes expected to be paid or accrued. The rules relating to the determination of the U.S. foreign tax credit are complex, and U.S. Holders should consult with their own tax advisors to determine whether, and to what extent, they are entitled to such credit. U.S. Holders that do not elect to claim a foreign tax credit may instead claim a deduction for Israeli income taxes withheld, provided such U.S. Holders itemize their deductions.

Disposition of Shares

Except as provided under the PFIC rules described below, upon the sale, exchange or other disposition of our Ordinary Shares, a U.S. Holder will recognize capital gain or loss in an amount equal to the difference between such U.S. Holder's tax basis in the sold Ordinary Shares and the amount realized on the disposition of such Ordinary Shares (or its U.S. dollar equivalent determined by reference to the spot rate of exchange on the date of disposition, if the amount realized is denominated in a foreign currency). The gain or loss realized on the sale or exchange or other disposition of Ordinary Shares will be long-term capital gain or loss if the U.S. Holder has a holding period of more than one year at the time of the disposition.

In general, gain realized by a U.S. Holder on a sale, exchange or other disposition of Ordinary Shares will generally be treated as U.S. source income for U.S. foreign tax credit purposes. A loss realized by a U.S. Holder on the sale, exchange or other disposition of Ordinary Shares is generally allocated to U.S. source income. However, U.S. Treasury Regulations require such loss to be allocated to foreign source income to the extent specified dividends were received by the taxpayer within the 24-month period preceding the date on which the taxpayer recognized the loss. The deductibility of a loss realized on the sale, exchange or other disposition of Ordinary Shares is subject to limitations.

Tax on Net Investment Income

U.S. Holders who are individuals, estates or trusts will generally be required to pay a new 3.8% tax on their net investment income (including dividends on and gains from the sale or other disposition of our Ordinary Shares), or in the case of estates and trusts, on their net investment income that is not distributed. In each case, this tax applies only to the extent that the U.S. Holder's total adjusted income exceeds applicable thresholds.

Passive Foreign Investment Companies

Special U.S. federal income tax laws apply to a U.S. Holder who owns shares of a corporation that was (at any time during the U.S. Holder's holding period) a PFIC. We would be treated as a PFIC for U.S. federal income tax purposes for any tax year if, in such tax year, either:

- 75% or more of our gross income (including our *pro rata* share of gross income for any company, U.S. or foreign, in which we are considered to own 25% or more of the shares by value), in a taxable year is passive (the "Income Test"); or
- At least 50% of our assets, averaged over the year and generally determined based upon value (including our *pro rata* share of the assets of any company in which we are considered to own 25% or more of the shares by value), in a taxable year are held for the production of, or produce, passive income (the "Asset Test").

For this purpose, passive income generally consists of dividends, interest, rents, royalties, annuities and income from certain commodities transactions and from notional principal contracts. Cash is treated as generating passive income.

If we are or become a PFIC, each U.S. Holder who has not elected to treat us as a qualified electing fund by making a "QEF election", or who has not elected to mark the shares to market (as discussed below), would, upon receipt of certain distributions by us and upon disposition of our Ordinary Shares at a gain, be liable to pay U.S. federal income tax at the then prevailing highest tax rates on ordinary income plus interest on such tax, as if the distribution or gain had been recognized ratably over the taxpayer's holding period for our Ordinary Shares. In addition, when shares of a PFIC are acquired by reason of death from a decedent that was a U.S. Holder, the tax basis of such shares would not receive a step-up to fair market value as of the date of the decedent's death, but instead would be equal to the decedent's basis if lower, unless all gain were recognized by the decedent. Indirect investments in a PFIC may also be subject to special U.S. federal income tax rules.

The PFIC rules described above would not apply to a U.S. Holder who makes a QEF election for all taxable years that such U.S. Holder has held our Ordinary Shares while we are a PFIC, provided that we comply with specified reporting requirements. Instead, each U.S. Holder who has made such a QEF election is required for each taxable year that we are a PFIC to include in income such U.S. Holder's *pro rata* share of our ordinary earnings as ordinary income and such U.S. Holder's *pro rata* share of our net capital gains as long-term capital gain, regardless of whether we make any distributions of such earnings or gain. In general, a QEF election is effective only if we make available certain required information. The QEF election is made on a shareholder-by-shareholder basis and generally may be revoked only with the consent of the IRS. Although we have no obligation to do so, we intend to comply with the applicable information reporting requirements for U.S. Holders to make a QEF election.

A U.S. Holder of PFIC shares which are traded on qualifying public markets, including the NASDAQ, can elect to mark the shares to market annually, recognizing as ordinary income or loss each year an amount equal to the difference as of the close of the taxable year between the fair market value of the PFIC shares and the U.S. Holder's adjusted tax basis in the PFIC shares. Losses are allowed only to the extent of net mark-to-market gain previously included income by the U.S. Holder under the election for prior taxable years.

In light of the complexity of PFIC rules, we cannot assure you that we have not been or are not a PFIC or will avoid becoming a PFIC in the future. U.S. Holders who hold Ordinary Shares during a period when we are a PFIC will be subject to the foregoing rules, even if we cease to be a PFIC, subject to specified exceptions for U.S. Holders who made a QEF or mark-to-market election. U.S. Holders are strongly urged to consult their tax advisors about the PFIC rules, including tax return filing requirements and the eligibility, manner, and consequences to them of making a QEF or mark-to-market election with respect to our Ordinary Shares in the event that we qualify as a PFIC. For those U.S. Holders who determine that we were a PFIC in any of our taxable years and notify us in writing of their request for the

information required in order to effectuate the QEF election described above, we will promptly make such information available to them.

Information Reporting and Withholding

A U.S. Holder may be subject to backup withholding at a rate of 28% with respect to cash dividends and proceeds from a disposition of Ordinary Shares. In general, back-up withholding will apply only if a U.S. Holder fails to comply with specified identification procedures. Backup withholding will not apply with respect to payments made to designated exempt recipients, such as corporations and tax-exempt organizations. Backup withholding is not an additional tax and may be claimed as a credit against the U.S. federal income tax liability of a U.S. Holder, provided that the required information is timely furnished to the IRS.

Under the Hiring Incentives to Restore Employment Act of 2010 (the "HIRE Act"), some payments made to "foreign financial institutions" in respect of accounts of U.S. stockholders at such financial institutions may be subject to withholding at a rate of 30%. U.S. Treasury Regulations provide that such withholding will only apply to distributions paid on or after January 1, 2014, and to other "withholdable payments" (including payments of gross proceeds from a sale or other disposition of our Ordinary Shares) made on or after January 1, 2017. U.S. Holders should consult their tax advisors regarding the effect, if any, of the HIRE Act on their ownership and disposition of our Ordinary Shares. See "Non-U.S. Holders of Ordinary Shares."

Non-U.S. Holders of Ordinary Shares

Except as provided below, an individual, corporation, estate or trust that is not a U.S. Holder generally will not be subject to U.S. federal income or withholding tax on the payment of dividends on, and the proceeds from the disposition of, our Ordinary Shares.

A non-U.S. Holder may be subject to U.S. federal income or withholding tax on a dividend paid on our Ordinary Shares or the proceeds from the disposition of our Ordinary Shares if: (1) such item is effectively connected with the conduct by the non-U.S. Holder of a trade or business in the United States or, in the case of a non-U.S. Holder that is a resident of a country which has an income tax treaty with the United States, such item is attributable to a permanent establishment or, in the case of gain realized by an individual non-U.S. Holder, a fixed place of business in the United States; (2) in the case of a disposition of our Ordinary Shares, the individual non-U.S. Holder is present in the United States for 183 days or more in the taxable year of the sale and other specified conditions are met; (3) the non-U.S. Holder is subject to U.S. federal income tax pursuant to the provisions of the U.S. tax law applicable to U.S. expatriates.

In general, non-U.S. Holders will not be subject to backup withholding with respect to the payment of dividends on our Ordinary Shares if payment is made through a paying agent or office of a foreign broker outside the United States. However, if payment is made in the United States or by a U.S. related person, non-U.S. Holders may be subject to backup withholding, unless the non-U.S. Holder provides on an applicable Form W-8 (or a substantially similar form) a taxpayer identification number, certifies to its foreign status, or otherwise establishes an exemption. A U.S. related person for these purposes is a person with one or more current relationships with the United States.

The amount of any backup withholding from a payment to a non-U.S. Holder will be allowed as a credit against such holder's U.S. federal income tax liability and may entitle such holder to a refund, provided that the required information is timely furnished to the IRS.

The HIRE Act may impose withholding taxes on some types of payments made to "foreign financial institutions" and some other non-U.S. entities. Under the HIRE Act, the failure to comply with additional certification, information reporting and other specified requirements could result in withholding tax being imposed on payments of dividends and sales proceeds to U.S. Holders that own Ordinary Shares through foreign accounts or foreign intermediaries and specified non-U.S. Holders. The HIRE Act imposes a 30% withholding tax on dividends on, and gross proceeds from the sale or other disposition of, Ordinary Shares paid from the United States to a foreign financial institution or to a foreign nonfinancial entity, unless (i) the foreign financial institution undertakes specified diligence and reporting obligations or (ii) the foreign nonfinancial entity either certifies it does not have any substantial U.S. owners or furnishes identifying information regarding each substantial U.S. owner. In addition, if the payee is a foreign financial

institution, it generally must enter into an agreement with the U.S. Treasury that requires, among other things, that it undertake to identify accounts held by specified U.S. persons or U.S.-owned foreign entities, annually report certain information about such accounts, and withhold 30% on payments to other specified account holders. U.S. Treasury Regulations provide that such withholding will only apply to distributions paid on or after January 1, 2014, and to other "withholdable payments" (including payments of gross proceeds from a sale or other disposition of our Ordinary Shares) made on or after January 1, 2017. You should consult your tax advisor regarding the HIRE Act.

Item 11. Quantitative and Qualitative Disclosures about Market Risk.

We develop our technology in Israel and in Germany and seek to provide our services worldwide. As a result, our foreign currency exposures give rise to market risk associated with exchange rate movements of the U.S. dollar, our functional and reporting currency, against the NIS and Euro. We are exposed to the risk of fluctuation in the U.S. dollar/NIS and the U.S. dollar/Euro exchange rate. Our NIS and Euro-denominated expenses consist principally of salaries and related personnel expenses. Although the majority of our revenues are in US dollars, a substantial portion of our sales are derived from the Euro currency. Neither a ten percent increase nor decrease in current exchange rates would have a material effect on our consolidated financial statements in the next six months.

Due to the fact that we do not have any material debt, we have concluded that there is currently no material interest market risk exposure.

Therefore, no quantitative tabular disclosures are provided.

Item 12. Description of Securities Other than Equity Securities.

The Company does not have any outstanding American Depositary Shares or American Depositary Receipts.

PART II

Item 13. Defaults, Dividend Arrearages and Delinquencies.

None.

Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds.

None.

Item 15. Controls and Procedures.

(a) As of December 31, 2012, we performed an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act). Our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and our management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective as of December 31, 2012, to provide reasonable assurance that the information required to be disclosed in filings and submissions under the Exchange Act, is recorded, processed, summarized, and reported within the time periods specified by the SEC's rules and forms, and that such information related to us and our consolidated subsidiary is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions about required disclosure.

(b) Our management is responsible for establishing and maintaining adequate internal control over our financial reporting, as such term is defined in Rule 13a-15 (f) under the Security Exchange Act. Our internal control over financial reporting system was 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 (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) 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 (iii) 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 and even when determined to be effective can only provide reasonable assurance with respect to financial statements. 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.

Our management assessed our internal control over financial reporting as of December 31, 2012. Our management based its assessment on criteria established in Internal Control- Integrated Framework issued by the Committee of Sponsoring Organization of the Treadway Commission. Based on this assessment, our management has concluded that, as of December 31, 2012, our internal control over financial reporting is effective.

This Annual Report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to a provision under the Dodd-Frank Wall Street Reform and Consumer Protection Act which grants a permanent exemption for non-accelerated filers from complying with Section 404(b) of the Sarbanes-Oxley Act of 2002.

(c) During the period covered by this Annual Report, there were no changes to our internal control over financial reporting that occurred during the year ended December 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 16A. Audit Committee Financial Expert.

The Board of Directors of the Company has determined that Mr. Todd Thomson, a member of the Audit Committee, is an "audit committee financial expert" as that term is defined in Item 16A of Form 20-F, and is "independent" as that term is defined in NASDAQ Listing Rule 5605(a)(2).

Item 16B. Code of Ethics.

The Company, by way of Board of Directors resolution, has adopted a Code of Ethics applicable to its senior financial officers, including its principal executive, financial and accounting officers. The Code of Ethics is posted on the Company's website at www.commtouch.com, under the tab for "Corporate Governance" located on the link to the "Investor Relations" page.

Item 16C. Principal Accountant Fees and Services.

Kost, Forer, Gabbay & Kasierer, a member of Ernst & Young Global, has served as our Independent Registered Public Accounting Firm for each of the fiscal years in the three-year period ended December 31, 2012, for which audited financial statements appear in this Annual Report. The following table presents the aggregate fees for professional and other services rendered by Kost, Forer, Gabbay & Kasierer for 2012 and 2011:

	Year ended December 31,	
	2012 Fees	2011 Fees
Audit fees (1)	$ 127,000	$ 132,000
Audit Related (2)	$ 74,000	-
Tax Fees (3)	$ 28,000	$ 28,000
Other	$ 40,000	$ -
Total	**$ 269,000**	**$ 160,000**

(1) Audit fees consist of fees billed for the annual audit services engagement and other audit services, which are those services that only the independent registered public accounting firm can reasonably provide, and include the group audit including statutory audits; consents; attest services; and assistance in connection with documents filed with the SEC.

(2) Audit-related fees relate to assurance and associated services that traditionally are performed by the independent auditor, including: accounting consultation and consultation concerning financial accounting, reporting standards and government approvals and due diligence investigations.

(3) Tax fees are for professional services rendered by our auditors for tax compliance, tax advice on actual or contemplated transactions, tax consulting associated with international transfer prices and global mobility of employees.

Audit Committee Pre-approval Policies and Procedures

Below is a summary of our current Policies and Procedures:

The main role of the Company's audit committee is to assist the Board of Directors in fulfilling its responsibility for oversight of the quality and integrity of the accounting, auditing and reporting practices of the Company. The Audit Committee oversees the appointment, compensation, and oversight of the Company's independent registered public accounting firm engaged to prepare or issue an audit report on the financial statements of the Company. The audit committee's specific responsibilities in carrying out its oversight role include the approval of all audit and non-audit services to be provided by the external auditor and the quarterly review of the firm's non-audit services and related fees. These services may include audit services, audit-related services, tax services and other services, as described above. It is the policy of the audit committee to approve in advance the particular services or categories of services to be provided to the Company periodically. Additional services may be pre-approved by the audit committee on an individual basis during the year. The audit committee did not avail itself of section (c)(7)(i)(C) of Rule 2-01 of Regulation S-X during 2012, which allows for an exemption from the pre-approval process under certain limited circumstances.

Item 16D. **Exemptions from the Listing Standards for Audit Committees.**

Not applicable.

Item 16E. **Purchases of Equity Securities by the Issuer and Affiliated Purchasers.**

Following completion of its Ordinary Share buyback plans during 2009 and 2010 (see Item 16E of the annual reports on Form 20-F filed for 2009 and 2010), in May 2012, the Company announced the commencement of its third Ordinary Share buyback plan, under which the Company purchased almost $2 million worth of its Ordinary Shares through the end of 2012 (out of a total amount allocated of $2.5 million). The Company completed this buyback plan in November 2012 and, in total, it expended $1.7 million to repurchase 600,337 Ordinary Shares at an average price of $2.79 per share. Repurchases during 2012 are summarized in the following table:

ISSUER PURCHASES OF SECURITIES DURING 2012

Period	Total Number Of Shares Purchased	Average Price Paid Per Share ($)	Total Number Of Shares Purchased As Part of Publicly Announced Plan	Maximum U.S. Dollar Value That May Yet Be Purchased Under The Plan
May 1 – May 31	62,494	2.7	62,494	2,331,418
June 1 – June 30	135,596	2.94	135,596	1,932,796
July 1 – July 31	130,209	2.69	130,209	1,582,571
August 1- August 31	113,451	2.91	113,451	1,251,942
September 1 – September 30	53,274	2.83	53,274	1,101,369
October 1 – October 31	76,254	2.59	76,254	904,089
November 1 – November 30	29,059	2.63	29,059	827,596
Total	600,337	2.79	600,337	N/A

Item 16F. Change in Registrant's Certifying Accountant.

Not applicable.

Item 16G. Corporate Governance.

Under NASDAQ Listing Rule 5615(a)(3), foreign private issuers, such as our Company, are permitted to follow certain home country corporate governance practices instead of certain provisions of certain NASDAQ Listing Rules. We do not comply with the following requirements of the NASDAQ Listing Rules, and instead follow Israeli law and practice with respect to such corporate governance practices:

NASDAQ Listing Rule 5250(d) requires that an annual report be delivered to shareholders in accordance with three alternative delivery methods set forth in the rule. One of those delivery methods allows for the posting of the annual report on the Company's website. However, that method also requires that i) a prominent undertaking be posted on the website indicating that, upon request, shareholders may receive a hard copy of the annual report free of charge, and ii) simultaneous with this posting, the Company issue a press release stating that its annual report has been filed with the SEC (or other appropriate regulatory authority). This press release must also state that the annual report is available on the Company's website and include the website address and that shareholders may receive a hard copy free of charge upon request.

While the Company's most current annual report on Form 20-F, inclusive of consolidated financial statements, is available on its website at www.commtouch.com, and the Company has indicated publicly that it will provide copies of that report free of charge, upon shareholder request, nevertheless the Company is not in strict compliance with the NASDAQ rule. The Company does not include a statement on its website in the form noted above and does not issue a press release upon the posting of the annual report to its website; rather, the Company is following its home country practice (in Israel, which, in addition to the Company's activities noted above, also enables shareholders to inspect the Company's annual consolidated financial statements in person at its principal offices).

Rule 5620(c) to NASDAQ Listing Rules requires that an issuer listed on NASDAQ have a quorum requirement that in no case be less than 33 1/3% of the outstanding shares of a company's common voting stock. However, the Company's articles of association, consistent with the Companies Law, provide for a lower quorum in the event of a meeting adjourned for lack of a quorum, in which case any two shareholders entitled to vote and present in person or by proxy at such adjourned meeting shall constitute a quorum. Our quorum requirements for an adjourned meeting do not comply with the NASDAQ requirements and we instead follow our home country practice.

Rule 5635(c) of the NASDAQ Listing Rules requires that, except in certain defined instances, an issuer receive shareholder approval prior to the issuance of securities when a stock option or purchase plan is to be established or materially amended or other equity compensation arrangement made or materially amended, pursuant to which stock may be acquired by officers, directors, employees, or consultants. During 2012, the Company notified NASDAQ that it is opting to follow home country practice in this regard. Under Israeli law, shareholder approval is not required for some of the matters listed under Rule 5635(c), and thus Board of Director approval, together with that of the Compensation Committee, will be sufficient to approve those matters. As noted above under Item 6, "*Compensation Committee*", the Company is planning to adopt a compensation policy focused on director, CEO and corporate officer compensation (hereinafter "executive compensation"). Pursuant to Israeli law, such policy must be presented to shareholders for approval prior to September 2, 2013. Included within that policy will be provisions relating to the equity component of executive compensation, so in relation to those provisions, the Company will continue to follow NASDAQ Listing Rules in seeking shareholder approval. As noted under Item 6, even if our shareholders fail to approve the compensation policy, the Board nevertheless is entitled to adopt such policy if it determines that it is in the best interests of the Company.

As a foreign private issuer listed on the NASDAQ Capital Market, we may also follow home country practice with regard to, among other things, composition of the board of directors, director nomination process and regularly scheduled meetings at which only independent directors are present. In addition, we may follow our home country practice, instead of the NASDAQ Listing Rules, which require that we obtain shareholder approval for certain dilutive events, such as an issuance that will result in a change of control of the company, certain transactions other than a public offering involving issuances of a 20% or more interest in the company and certain acquisitions of the stock or assets of another company. A foreign private issuer that elects to follow a home country practice instead of NASDAQ requirements, must submit to NASDAQ in advance a written statement from an independent counsel in such issuer's home country certifying that the issuer's practices are not prohibited by the home country's laws. In addition, a foreign private issuer must disclose in its annual reports filed with the Securities and Exchange Commission or on its website each such requirement that it does not follow and describe the home country practice followed by the issuer instead of any such requirement. Accordingly, our shareholders may not be afforded the same protection as provided under NASDAQ's corporate governance rules.

Item 16H. Mine Safety Disclosure.

Not applicable.

PART III

Item 17. Financial Statements.

The Company has responded to Item 18

Item 18. Financial Statements.

See pages F-1 to F-31.

COMMTOUCH SOFTWARE LTD. AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2012

U.S. DOLLARS IN THOUSANDS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

COMMTOUCH SOFTWARE LTD.

We have audited the accompanying consolidated balance sheets of Commtouch Software Ltd. ("the Company") and its subsidiaries as of December 31, 2011 and 2012, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2012. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2011 and 2012, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2012, in conformity with U.S. generally accepted accounting principles.

Tel-Aviv, Israel
April 25, 2013

/s/ KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

CONSOLIDATED BALANCE SHEETS
U.S. dollars in thousands

	December 31	
	2011	**2012**
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 20,868	$ 5,137
Trade receivables, net	2,838	5,996
Deferred income taxes	1,996	2,239
Prepaid expenses and other accounts receivable	463	1,503
Total current assets	26,165	14,875
LONG-TERM ASSETS:		
Investment in affiliates	1,227	1,403
Deferred income taxes	2,889	3,348
Intangible assets, net	3,505	14,568
Goodwill	3,792	22,518
Severance pay fund	1,031	756
Lease deposits	40	57
Property and equipment, net	885	1,608
Total long-term assets	13,369	44,258
Total assets	$ 39,534	$ 59,133

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

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands, except share and per share data

	December 31	
	2011	**2012**
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 551	$ 958
Employees and payroll accruals	1,215	2,280
Accrued expenses and other liabilities	628	1,587
Earn-out consideration	3,372	4,048
Deferred revenues	3,058	4,535
Total current liabilities	8,824	13,408
LONG-TERM LIABILITIES:		
Long-term deferred revenues	694	492
Earn-out consideration	-	6,409
Deferred tax liability	-	3,187
Accrued severance pay	1,192	915
Total long-term liabilities	1,886	11,003
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY:		
Ordinary shares nominal value NIS 0.15 par value- Authorized: 55,353,340 shares as of December 31, 2011 and 2012; Issued: 27,287,909 and 27,915,392 shares as of December 31, 2011 and 2012, respectively; Outstanding: 24,093,617 and 25,826,234 shares as of December 31, 2011 and 2012, respectively	960	986
Additional paid-in capital	188,463	190,436
Treasury shares 3,194,292 Ordinary shares as of December 31, 2011 and 2,089,158 ordinary shared as of December 31, 2012	(8,692)	(6,653)
Accumulated other comprehensive income	23	469
Accumulated deficit	(151,930)	(150,516)
Total shareholders' equity	28,824	34,722
Total liabilities and shareholders' equity	$ 39,534	$ 59,133

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

CONSOLIDATED STATEMENTS OF INCOME

U.S. dollars in thousands, except share and per share data

	Year ended December 31,		
	2010	**2011**	**2012**
Revenues	$ 18,161	$ 23,016	$ 23,910
Cost of revenues	2,918	4,091	4,350
Gross profit	15,243	18,925	19,560
Operating expenses:			
Research and development, net	3,397	5,410	6,281
Sales and marketing	4,575	5,486	5,860
General and administrative	3,911	4,721	6,639
Total operating expenses	11,883	15,617	18,780
Operating income	3,360	3,308	780
Financial income (expenses), net	(55)	(27)	80
Income before taxes	3,305	3,281	860
Tax benefit	1,098	1,317	625
Net income	$ 4,403	$ 4,598	$ 1,485
Basic net earnings per share	$ 0.19	$ 0.19	$ 0.06
Diluted net earnings per share	$ 0.18	$ 0.19	$ 0.06
Weighted average number of shares used in computing basic net earnings per share	23,575,354	23,620,171	24,610,267
Weighted average numbers of shares used in computing diluted net earnings per share	24,873,778	24,654,458	25,140,439

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

U.S. dollars in thousands, except share and per share data

	Year ended December 31,		
	2010	**2011**	**2012**
Net Income	$ 4,403	$ 4,598	$ 1,485
Other comprehensive income:			
Foreign currency translation adjustments	-	-	446
Other comprehensive income	$ -	$ -	$ 446
Total comprehensive income	$ 4,403	$ 4,598	$ 1,931

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share data

	Number of Ordinary shares	Ordinary shares amount	Additional paid-in capital	Treasury stock	Accumulated other comprehensive income *)	Accumulated deficit	Total
Balance as of January 1, 2010	23,958,761	$ 926	$ 183,731	$ (4,872)	$ 23	$ (160,931)	$ 18,877
Purchase of treasury shares	(1,030,466)	-	-	(3,820)	-	-	(3,820)
Issuance of shares upon exercise of options and warrants	577,418	12	785	-	-	-	797
Stock-based compensation related to employees	-	-	1,465	-	-	-	1,465
Stock-based compensation related to options granted to non-employees	-	-	31	-	-	-	31
Net income	-	-	-	-	-	4,403	4,403
Balance as of December 31, 2010	23,505,713	938	186,012	(8,692)	23	(156,528)	21,753
Issuance of shares upon exercise of options and warrants	587,904	22	1,238	-	-	-	1,260
Stock-based compensation related to employees	-	-	1,213	-	-	-	1,213
Net income	-	-	-	-	-	4,598	4,598
Balance as of December 31, 2011	24,093,617	960	188,463	(8,692)	23	(151,930)	28,824
Purchase of treasury shares	(600,337)	-	-	(1,720)	-		(1,720)
Issuance of shares upon exercise of options	627,483	26	686	-	-	-	712
Issuance of treasury shares upon acquisitions	1,556,750	-	104	3,406	-	-	3,510
Issuance of treasury shares upon exercise of options	148,721	-	(104)	353	-	(71)	178
Stock based compensation related to options granted to non-employees	-	-	11	-	-	-	11
Other comprehensive income	-	-	-	-	446	-	446
Stock-based compensation related to employees	-	-	1,276	-	-	-	1,276
Net income	-	-	-	-	-	1,485	1,485
Balance as of December 31, 2012	25,826,234	$ 986	$ 190,436	$ (6,653)	$ 469	$ (150,516)	$ 34,722

*) Relates to foreign currency translation adjustments

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2010	**2011**	**2012**
Cash flows from operating activities:			
Net income	$ 4,403	$ 4,598	$ 1,485
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation	520	545	560
Compensation related to options granted to employees and non-employees	1,496	1,213	1,287
Amortization and impairment of intangible assets	158	1,005	589
Increase in deferred income taxes	(1,096)	(1,385)	(806)
Capital gain from sale of equipment	(9)	-	-
Changes in assets and liabilities:			
Decrease (increase) in trade receivables	(1,036)	130	(2,194)
Decrease (increase) in prepaid expenses and other accounts receivable	287	(79)	(541)
Increase in accounts payable	138	17	300
Increase in employees and payroll accruals, accrued expenses and other liabilities	163	981	(861)
Decrease in deferred revenues	(697)	(390)	(164)
Increase (decrease) in accrued severance pay, net	(10)	66	(2)
Net cash provided by (used in) operating activities	4,317	6,701	(347)
Cash flows from investing activities:			
Decrease (Increase) in long-term lease deposits	22	1	(17)
Payment for business acquisitions, net of cash acquired	(4,600)	-	(10,243)
Investment in affiliate	-	-	(176)
Proceeds from sale of equipment	9	-	-
Purchase of property and equipment	(568)	(526)	(805)
Net cash used in investing activities	(5,137)	(525)	(11,241)

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2010	**2011**	**2012**
Cash flows from financing activities:			
Purchase of treasury shares at cost	(3,820)	-	(1,720)
Contingent payment of acquisition	-	-	(3,400)
Proceeds from options and warrants exercised	797	1,260	890
Net cash provided by (used in) financing activities	(3,023)	1,260	(4,230)
Increase (decrease) in cash and cash equivalents	(3,843)	7,436	(15,818)
Effect of exchange rate changes on cash	-	-	87
Cash and cash equivalents at the beginning of the year	17,275	13,432	20,868
Cash and cash equivalents at the end of the year	$ 13,432	$ 20,868	$ 5,137
Supplemental disclosure of cash flows activities:			
Cash paid during the year for:			
Taxes paid	$ -	$ 67	$ 148
Non-cash transactions:			
Purchase of property and equipment - trade payables	$ (55)	$ (16)	(48)

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL

a. Commtouch Software Ltd. ("Commtouch" or the Company") was incorporated under the laws of Israel in 1991. The Company and its subsidiaries develop and provide internet security solutions to OEM partners and enterprises. The Company's business is to develop and sell, through a variety of third party distribution channels, these solutions to various customers. The Company's messaging solutions are comprised of anti-spam, Zero-Hour Virus Outbreak Detection and GlobalView Mail Reputation solutions, its Web security solution is known as GlobalView URL filtering, and its antivirus solution is known as Command Antivirus. The Company operates in one reportable segment.

b. The Company expects that it will continue to be dependent upon third-party distribution channels for a significant portion of its revenues, which are expected to be derived from sales of the Company's anti-spam, Zero-Hour, anti-virus, IP reputation, URL filtering solutions and Command Antivirus.

c. On October 1, 2012, the Company completed the acquisition of the antivirus business of Frisk Software, an Incorporated Icelandic private limited company, or "Frisk". The acquisition accelerated Commtouch's antivirus roadmap and enabled the Company to more quickly provide the most advanced antivirus technology utilizing the combined resources of both organizations. It also helps support the launch of private label antivirus solution for the OEM and service provider markets while also enhancing the company's Saas Capabilities.

The purchase price amounted to $4,915 out of which $2,200 was paid in cash at the closing date, $1,678 was paid by issuance of 750,000 ordinary shares. An additional contingent consideration in an estimated fair value of $1,037 will be paid based on future revenues. The earn out payment will be based on revenues for each of the years ended December 31, 2012 December 31, 2013 and December 31, 2014 and in respect of the First quarter of 2015.

The total purchase price was allocated to the net tangible and identifiable intangible assets on their estimated fair values at the acquisition date as set forth below. The excess of the purchase price over the net tangible and identifiable intangible assets was to goodwill. The value of goodwill is attributed to operational synergies between Commtouch and Frisk and to the strengthening of the Company's position in the market.

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL (Cont.)

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed:

Cash	$ 202
Trade receivables	36
Other receivables and prepaid expenses	287
Property and equipment	64
Other intangible assets	2,250
Goodwill	3,501
Total assets acquired	6,340
Trade payables	(571)
Deferred revenues	(565)
Long-term deferred tax liabilities	(289)
Total liabilities assumed	(1,425)
Net assets acquired	$ 4,915

Intangible assets that are subject to amortization are amortized over their estimated useful lives using the straight-line method at an annual weighted average rate of 8%. The following table sets forth the components of intangible assets associated with the acquisition and their annual rates of amortization:

	Fair value	%
Trademark	$ 984	10
Intellectual Property	1,266	6.7
Total intangible assets	$ 2,250	

d. Acquisition of Eleven GMBH:

On November 16, 2012, the Company completed the acquisition of Eleven GMBH, Germany based company, or “Eleven”.

Eleven is well known throughout Germany as the leading provider of mail - based security as a service (SecaaS) solutions.

The acquisition of eleven enables Commtouch to accelerate delivery of private label cloud - based security solutions specifically designed for OEM and service provider markets. In addition, Commtouch’s global reach should accelerate sales and adoption of this leading security technology developed by eleven.

The purchase price amounted to $22,293 out of which, $11,543 was paid in cash at the closing date.

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL (Cont.)

$1,832 was paid by issuance of 806,750 ordinary shares. An additional contingent consideration in an estimated fair value of $8,918 will be paid based on the business revenues from 2012 to 2015.

The total purchase price was allocated to the company's business net tangible and identifiable assets based on their estimated fair values at the acquisition date as set forth below. The excess of the purchase price over the net tangible and identifiable intangible assets was assigned to goodwill. The value of goodwill is attributed to synergies between Commtouch and Eleven's services and the strength of the Company's position in the market.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed:

Cash	$	3,297
Trade receivables		846
Other receivables and prepaid expenses		252
Property and equipment		449
Other intangible assets		9,100
Goodwill		14,732
Total assets acquired		28,676
Trade payables		(128)
Employees and payroll accruals		(194)
Accrued expenses and other liabilities		(2,313)
Deferred revenues		(844)
Long-term deferred tax liabilities		(2,904)
Total liabilities assumed		(6,383)
Net assets acquired	$	22,293

The Intangible assets that are subject to amortization are amortized over their estimated useful lives using the straight-line method at an annual weighted average rate of 10%, except for customer relations which is amortized on an accelerated basis.

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL (Cont.)

The following table sets forth the components of intangible assets associated with the acquisition and their annual rates of amortization:

	Fair value	%
Trademark	671	10
Customer relations	3,037	Accelerated method
Technology	4,611	10
In Process R&D *	781	(*)
Total intangible assets	$ 9,100	

(*) The In Process R&D will be amortized when the development will be completed.

Unaudited pro forma condensed results of income:

The following represents the unaudited pro forma condensed results of income for the years ended December 31, 2012 and 2011, assuming that the acquisition occurred on January 1, 2011. The pro forma information is not necessarily indicative of the results of operations that would have actually occurred had the acquisition been consummated on those dates, nor does it purport to represent the results of income for future periods.

	Year ended December 31,	
	2011	2012
	Unaudited	Unaudited
Revenues	$ 31,748	$ 31,203
Net income	$ 4,102	$ 1,048
Basic net earnings per share	$ 0.17	$ 0.04
Diluted net earnings per share	$ 0.16	$ 0.04

f. Acquisitions in previous years:

In 2010, the Company completed the acquisition of the assets of the Antivirus business of Authentium Inc. (subsequently known as SafeCentral Inc.). Total fair value of purchase consideration for the acquisitions was $ 7,431, which includes cash paid and estimated fair value of earn-out payment. In connection with this acquisition, the Company recorded intangibles and goodwill in the amounts of $ 4,663 and $ 3,792, respectively. In 2012, the Company paid an additional amount of $ 3,400 based on the Antivirus business's 2011 revenues.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP").

a. Use of estimates:

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. On an ongoing basis, the Company's management evaluates estimates. Such estimates are based on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities.

b. Financial statements in U. S. dollars:

The currency of the primary economic environment in which the operations of Commtouch and certain subsidiaries are conducted is the U.S. dollar ("dollar"); thus, the dollar is the functional currency of Commtouch and certain subsidiaries.

Commtouch and certain subsidiaries' transactions and balances denominated in dollars are presented at their original amounts. Non-dollar transactions and balances have been re-measured to dollars in accordance with ASC 830, "Foreign Currency Matters". All transaction gains and losses from re-measurement of monetary balance sheet items denominated in non-dollar currencies are reflected in the statements of income as financial income or expenses, as appropriate.

For those subsidiaries whose functional currency has been determined to be their local currency, assets and liabilities are translated at year-end exchange rates and statement of income items are translated at average exchange rates prevailing during the year. Such translation adjustments are recorded as a separate component of accumulated other comprehensive income (loss) in shareholders' equity.

c. Principles of consolidation:

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

d. Cash equivalents:

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

U.S. dollars in thousands, except share and per share data

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

e. Restricted cash:

The Company maintains certain cash amounts restricted as to withdrawal or use. On December 31, 2012, the Company maintained a balance of $122 that represents security deposits with respect to leases, restricted due to the lease agreement and security deposits for credit lines from banks. Restricted cash is presented within the prepaid expenses and other accounts receivable balance.

f. Investment in affiliates:

The Company's investments in affiliated companies comprises of investments in which the Company owns less than 20% and in which the Company cannot exercise significant influence over the affiliates' operating and financial policies are stated at cost.

The Company's investments are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an investment may not be recoverable. As of December 31, 2012 and 2011, the Company's investments are accounted for on a cost basis and no impairment losses have been identified.

g. Property and equipment:

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is calculated using the straight line method over the estimated useful lives of the assets at the following annual rates:

	%
Computers and peripheral equipment	33.33
Office furniture and equipment	7 – 20
Motor vehicles	15
Leasehold improvements	Over the shorter of the term of the lease or the life of the assets

Impairment of long-lived assets:

The Company and its subsidiaries long-lived assets and certain identifiable intangibles are reviewed for impairment in accordance with ASC 360 "Property, Plant and Equipment", 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 the future undiscounted cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. No impairment losses were recorded in 2010 through 2012.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

h. Goodwill:

Goodwill and certain other purchased intangible assets have been recorded as a result of acquisitions made in 2010 and in 2012. Goodwill represents the excess of the purchase price in a business combination over the fair value of net tangible and intangible assets acquired. Goodwill is not amortized, but rather is subject to an impairment test. The Company performs an annual impairment test at December 31, of each fiscal year, or more frequently if impairment indicators are present. The Company operates in one operating segment, and this segment comprises its only reporting unit.

ASC 350 prescribes a two-phase process for impairment testing of goodwill. The first phase screens for impairment, while the second phase (if necessary) measures impairment. Goodwill impairment is deemed to exist if the net book value of a reporting unit exceeds its estimated fair value determined using market capitalization. In such case, the second phase is then performed, and the Company measures impairment by comparing the carrying amount of the reporting unit's goodwill to the implied fair value of that goodwill. An impairment loss is recognized in an amount equal to the excess. For each of the three years in the period ended December 31, 2012, no impairment losses have been identified.

i. Intangible assets:

Intangible assets that are not considered to have an indefinite useful life are amortized over their estimated useful lives, which range from 8 to 15 years. Acquired customer contracts and relationships are amortized over their estimated useful lives in proportion to the economic benefits realized. This accounting policy results in accelerated amortization of such customer contracts and relationships arrangements as compared to the straight-line method. Technology & IP and Trademark are amortized over their estimated useful lives on a straight-line basis.

The IP R&D will be amortized to cost of goods sold when the acquired technology development will be completed.

The carrying amount of these assets to be held and used is reviewed whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of these assets is measured by comparison of the carrying amount of each asset (or asset group) to the future undiscounted cash flows the asset (or asset group) is expected to generate. If the asset is considered to be impaired, the amount of any impairment is measured as the difference between the carrying value and the fair value of the impaired asset.

During 2012 and 2010, no impairment losses have been identified. In 2011, impairment losses of $502 were recorded in respect of covenants not to compete.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

j. Fair value measurements:

Concurrently with the adoption of ASC 820, the Company adopted ASC Topic 825, "Financial Instruments," ("ASC 825") which permits entities to elect, at specified election dates, to measure eligible financial instruments at fair value. As of December 31, 2011 and 2012, the Company did not elect the fair value option under ASC 825 for any financial assets and liabilities that were not previously measured at fair value.

The carrying amounts of cash and cash equivalents, trade receivables, prepaid expenses, other accounts receivable and accounts payable, approximate their fair values due to the short-term maturities of financial instruments.

k. Revenue recognition:

The Company derives its revenues from the delivery of services of real-time Inbound Anti-Spam, Outbound Spam Protection for service providers, Zero-Hour Virus Outbreak Detection, GlobalView Mail Reputation, Command Antivirus, GlobalView URL Filtering and recently from Email Security SaaS (which is comprised of inbound and outbound anti-spam, plus antivirus) and Email Security On-Premise.

Revenue is recognized when there is a persuasive evidence of an arrangement, the service has been rendered, the collection of the fee is probably and the amount of fees to be paid by the customer is fixed or determinable.

Revenues from such services are recognized ratably over the contractual service term, which generally includes a term period of one to three years.

Deferred revenues include unearned amounts received from customers, but not yet recognized as revenues.

l. Research and development costs:

Research and development costs are charged to statements of income as incurred.

ASC 985-20, "Costs of Software to be Sold, Leased or Marketed", requires capitalization of certain software development costs subsequent to the establishment of technological feasibility.

Based on the Company's product development process, technological feasibility is established upon completion of a working model. Costs incurred by the Company between completion of the working models and the point at which the products are ready for general release, have been insignificant. Therefore, all research and development costs have been expensed.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

m. Government grants:

Royalty-bearing grants from the Government of Israel for funding certain approved research and development projects are recognized at the time the Company is entitled to such grants, on the basis of the related costs incurred and recorded as a deduction of research and development costs. Research and development grants from the Government of Israel amounted to $257, $131 and $774 in 2012, 2011 and 2010, respectively. See Note 5a.

n. Concentrations of credit risk:

The Company and its subsidiaries have no significant off-balance-sheet concentration of credit risk.

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables and cash and cash equivalents. The majority of the Company's cash and cash equivalents are invested in dollars and are deposited in major banks in the United States, Germany, Iceland and Israel. Such investments in the United States may be in excess of insured limits and are not insured in other jurisdictions. Management believes that the financial institutions that hold the Company's investments are institutions with high credit standing, and accordingly, minimal credit risk exists with respect to these investments.

The trade receivables of the Company are derived from transactions with companies located primarily in North America, Europe, Israel and Asia. An allowance for doubtful accounts is determined with respect to those amounts that the Company and its subsidiaries have determined to be doubtful of collection. The provision for doubtful accounts amounted to $32 and $462 at December 31, 2011 and 2012 respectively. Bad debt expense for each of the years ended December 31, 2010, 2011 and 2012 was $77, $7 and $456, respectively.

o. Accounting for stock-based compensation:

ASC 718 - "Compensation-stock Compensation"- ("ASC 718") requires companies to estimate the fair value of equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company's consolidated statements of income.

The Company recognizes compensation expense for the value of its awards on a straight line basis over the requisite service period of each of the awards, net of estimated forfeitures. Estimated forfeitures are based on actual historical pre-vesting forfeitures. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

U.S. dollars in thousands, except share and per share data

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company estimates the fair value of stock options granted using the Black-Scholes option-pricing model. The option-pricing model requires a number of assumptions, of which the most significant are the expected stock price volatility and the expected option term. Expected volatility was calculated based upon actual historical stock price movements. The expected term of options granted represents the period of time that options granted are expected to be outstanding, based upon historical experience. The risk-free interest rate is based on the yield from U.S. treasury bonds with an equivalent term. The Company has historically not paid dividends and has no foreseeable plans to pay dividends.

The Company applies ASC 718, and ASC 505-50, "Equity Based Payments to Non Employees" ("ASC 505-50"), with respect to options issued to non-employees.

The fair value for options granted in 2010, 2011 and 2012 is estimated at the date of grant using a Black-Scholes options pricing model with the following assumptions:

	Year ended December 31,		
Employee stock options	**2010**	**2011**	**2012**
Volatility	71%-73%	68%-70%	38%-51%
Risk-free interest rate	1.1%-1.6%	0.6%-2.1%	0.5%-0.9%
Dividend yield	0%	0%	0%
Expected term (years)	3.7-4.6	3.6-4.8	3.8-4.9

p. Basic and diluted net earnings per share:

Basic and diluted net earnings per share are presented in accordance with ASC 260, "Earnings per Share", for all periods presented.

Basic net earnings per share have been computed using the weighted-average number of Ordinary shares outstanding during the year. Diluted net earnings per share is computed based on the weighted average number of Ordinary shares outstanding during each year, plus the weighted average number of dilutive potential Ordinary shares considered outstanding during the year.

In 2010, 2011 and 2012, the difference between the denominator of basic and diluted net earnings per share is due to the effect of dilutive securities for stock options and warrants. In 2010, 2011 and 2012 1,211,247, 1,034,288 and 530,172, respectively, weighted average number of shares related to options and warrants outstanding were excluded from calculation of the diluted earnings per share since they would have an anti-dilutive effect.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

q. Severance pay:

The Company's liability for severance pay in Israel is calculated pursuant to Israel's Severance Pay Law based on the most recent salary of the employees multiplied by the number of years of employment as of the balance sheet date. Employees are entitled to one month's salary for each year of employment or a portion thereof. The Company's obligation for all of its Israeli employees is fully provided by monthly deposits with severance pay funds and insurance policies, and by an accrual. The value of those funds and policies is recorded as an asset in the Company's balance sheet.

The deposited funds include profits and losses accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfillment of the obligation pursuant to Israel's Severance Pay Law or labor agreements. The value of the deposited funds is based on the cash surrendered value of these policies.

Severance expense (income) for the years ended December 31, 2010, 2011 and 2012 was approximately $ (10), $ 66 and $ (2), respectively.

r. Treasury shares:

The Company repurchases its Ordinary shares from time to time on the open market and holds such shares as Treasury shares. The Company presents the cost to repurchase Treasury shares as a reduction in shareholders' equity.

The Company reissues treasury shares under the stock purchase plan, upon exercise of option and upon issuance of shares upon acquisitions. Reissuance of treasury shares is accounted for in accordance with ASC 505-30 whereby gains are credited to additional paid-in capital and losses are charged to additional paid-in capital to the extent that previous net gains are included therein; otherwise to retained earnings.

s. Income taxes:

The Company accounts for income taxes in accordance with ASC740, "Income Taxes" ("ASC 740"). ASC 740 prescribes the use of the liability method whereby deferred tax asset and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company provides a valuation allowance, if necessary, to reduce deferred tax assets to amounts more likely than not to be realized.

Deferred tax assets are classified as current or non-current based on the classification of the related asset or liability for financial reporting, or according to the expected reversal dates of the specific temporary differences if not related to an asset or liability for financial reporting.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

ASC 740 contains a two-step approach to recognizing and measuring a liability for uncertain tax positions. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. No liability for unrecognized tax benefits was recorded as a result of the implementation of ASC 740.

t. Comprehensive income:

The Company accounts for comprehensive income in accordance with ASC No. 220, "Comprehensive Income". Comprehensive income generally represents all changes in shareholders' equity during the period except those resulting from investments by, or distributions to, shareholders. The Company determined that its items of other comprehensive income relate to gains and losses from functional currency translation adjustments on behalf of subsidiaries whose functional currency has been determined to be their local currency.

u. Recently issued accounting pronouncements:

In February 2013, the FASB issued ASU No. 2013-02, "Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income." Under ASU 2013-02, an entity is required to provide information about the amounts reclassified out of Accumulated Other Comprehensive Income ("AOCI") by component. In addition, an entity is required to present, either on the face of the financial statements or in the notes, significant amounts reclassified out of AOCI by the respective line items of net income, but only if the amount reclassified is required to be reclassified in its entirety in the same reporting period. For amounts that are not required to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures that provide additional details about those amounts. ASU 2013-02 does not change the current requirements for reporting net income or other comprehensive income in the financial statements. ASU 2013-02 is effective for the Company as of January 1, 2013. Since this standard only impacts presentation and disclosure requirements, its adoption will not have a material impact on the Company's consolidated results of operations or financial condition.

U.S. dollars in thousands, except share and per share data

NOTE 3: PROPERTY AND EQUIPMENT, NET

	December 31	
	2011	2012
Cost:		
Computers and peripheral equipment	$ 4,717	$ 5,848
Office furniture and equipment	640	848
Motor vehicles	45	10
Leasehold improvements	1,195	1,225
	6,597	7,931
Less accumulated depreciation	(5,712)	(6,323)
Property and Equipment, net	$ 885	$ 1,608

Depreciation expense amounted to approximately $520, $545 and $560 in 2010, 2011 and 2012, respectively.

NOTE 4:- INTANGIBLE ASSETS, NET

a. Definite-lived other intangible assets:

	December 31,	
	2011	2012
Original amounts:		
Customer contracts and relationships	$ 2,476	$ 5,614
Technology	1,546	7,576
Covenants not-to-compete	646	-
Trademarks	-	1,677
In Process R&D	-	807
	4,668	15,674
Accumulated amortization:		
Customer contracts and relationships	260	542
Technology	257	531
Covenants not-to-compete	(*)646	-
Trademarks	-	33
In Process R&D	-	-
	1,163	1,106
Other intangible assets, net	$ 3,505	$ 14,568

(*) Includes write-off of covenants not-to-compete of $502 for the year ended December 31, 2011.

U.S. dollars in thousands, except share and per share data

NOTE 4:- INTANGIBLE ASSETS, NET (Cont.)

b. Amortization expense amounted to $ 158, $ 503 and $ 589 for 2010, 2011 and 2012, respectively.

NOTE 5:- GOODWILL

The changes in the carrying amount of goodwill for the year ended December 31, 2011 and 2012 are as follows:

	Year ended December 31,	
	2011	2012
Balance at the beginning of the year	$ 3,792	$ 3,792
Acquisitions	-	18,232
Functional currency translation adjustments	-	494
Balance at the year end	$ 3,792	$ 22,518

NOTE 6: COMMITMENTS AND CONTINGENCIES

a. Commtouch Software Ltd., which was incorporated in Israel, partially financed its research and development expenditures under programs sponsored by the Office of Chief Scientist ("OCS") for the support of certain research and development activities conducted in Israel.

In connection with its research and development, the Company received $ 1,354 of participation payments from the OCS. In return for the OCS's participation, the Company is committed to pay royalties at a rate of 3% of sales of the developed product, up to 100% of the amount of grants received (100% plus interest at LIBOR). The Company's total commitment for royalties payable with respect to future sales, based on OCS participations received or accrued, net of royalties paid or accrued, totaled approximately $ 1,210 as of December 31, 2012. For the years ended December 31, 2012, 2011 and 2010, the amounts of $ 58, $ 61 and $ 17, respectively, were recorded as cost of revenues with respect to royalties due to the OCS.

b. Operating leases:

The Company leases its facility in Israel under an operating lease agreement expiring on April 30, 2018. The subsidiaries in Iceland and Germany lease their facilities in Iceland and in Germany under operating lease agreements expiring on September 30, 2016 and December 31, 2015, respectively.

U.S. dollars in thousands, except share and per share data

NOTE 6: COMMITMENTS AND CONTINGENCIES (Cont.)

The US subsidiary leases its facilities in California, Florida and Washington D.C under operating lease agreements expiring on April 16, 2016, August 31, 2013 and February 28, 2015, respectively

Facilities rent expense for 2010, 2011 and 2012 was approximately $352, $410 and $531, respectively.

Annual minimum future lease payments due under the above agreements (and motor vehicle leases, which expire in 2013), at the exchange rate in effect on December 31, 2012, are approximately as follows:

2013	$	1,033
2014		952
2015		835
2016		461
2017		330
2018		110
	$	3,721

c. (1) During late 2010, one of the Company's customers, among others, was named as a defendant in a patent infringement claim in a United States District Court involving four distinct patents. In September 2011, the Company received an indemnification notification from the customer indicating that one or two of those patents may relate to Commtouch technology, and the customer was reserving its rights. During early 2013, the Company learned that its customer is negotiating a settlement of the matter, and the Company has been asked to contribute a portion towards the settlement. It is too early in the negotiations process to anticipate the outcome of the settlement negotiations and the Company possible contribution towards any final settlement.

(2) In December 2012, the U.S. subsidiary of the Company filed a lawsuit in the Superior Court of the State of California against one of its customers. The lawsuit includes a claim for breach of contract. In mid-April 2013, the customer filed its formal answer and a cross-complaint to the Company's complaint. The Company's lawsuit alleges damages in excess of $7,000, while the customer's cross-complaint does not set forth a fixed amount that it is seeking. It is expected that the discovery phase of the litigation will commence in the near future.

NOTE 7: SHAREHOLDERS' EQUITY

a. General:

Ordinary shares confer upon their holders the right to receive notice to participate and vote in general shareholder meetings of the Company and to receive dividends, if declared.

b. Employee stock options:

In 1996, the Company adopted the 1996 CSI Stock Option Plan for granting options to its U.S. employees and consultants to purchase Ordinary shares of the Company, which was replaced in 2006 by the 2006 U.S. Stock Option Plan. Until 1999, the Company issued options to purchase Ordinary shares to its Israeli employees pursuant to individual agreements. In 1999, the Company approved the 1999 Section 3(i) share option plan for its Israeli employees and consultants, (which was amended in 2003 and renamed the "Amended and Restated Israeli Share Option Plan"). As of December 31, 2011, an aggregate of 1,544,033 Ordinary shares of the Company are still available for future grant to employees and directors.

Options granted under such plans and agreements through September 2005, generally expire after ten years from the date of grant and options granted after September 2005 generally expire six-years from the date of grant. Options cease vesting upon termination of the optionee's employment or other relationship with the Company. The options generally vest over a period of four years. The exercise price of the options granted under the individual agreements may not be less than the nominal value of the shares into which such options are exercisable. Any options that are canceled or not exercised within the option term become available for future grant.

U.S. dollars in thousands, except share and per share data

NOTE 7: SHAREHOLDERS' EQUITY (Cont.)

A summary of the Company's employees share option activity under the plans is as follows:

	Number of options	Weighted average exercise price	Aggregate intrinsic value
	2012	2012	2012
Outstanding at the beginning of the year	4,032,681	$ 3.06	$ 2,554
Granted	1,716,552	2.65	
Exercised	(738,995)	1.05	
Expired and forfeited	(1,018,770)	3.92	
Outstanding at the end of the year	3,991,468	$ 3.03	$ 1,525
Options vested and expected to vest at the end of the year	3,800,579	$ 3.03	$ 1,462
Exercisable options at the end of the year	1,401,584	$ 3.28	$ 727
Weighted average fair value of options granted during the year	-	$ 2.88	-

The aggregate intrinsic value of the Company's options is the difference between (i) the Company's closing share price on the last trading day of the fiscal year 2012 and (ii) the exercise price, times the number of options.

As of December 31, 2012, the Company had approximately $3,174 of unrecognized compensation expense related to non-vested stock options, expected to be recognized over a period of 4.25 years.

U.S. dollars in thousands, except share and per share data

NOTE 7: SHAREHOLDERS' EQUITY (Cont.)

The options outstanding as of December 31, 2012, have been separated into ranges of exercise prices, as follows:

Exercise price per share	Options outstanding	Weighted average remaining contractual life in years	Weighted average price per share	Options exercisable	Weighted average exercise price per share of exercisable options
$0.93-$1.89	283,784	1.93	$ 1.33	283,784	$ 1.33
$1.93-$2.44	778,219	5.22	2.35	148,125	1.98
$2.46-$2.92	956,500	4.74	2.64	162,500	2.74
$3.12-$3.14	36,948	4.38	3.17	29,325	3.17
$3.16-$3.18	248,000	5.13	3.16	-	-
$3.21-$3.28	555,000	4.81	3.21	161,858	3.21
$3.41-$3.69	583,000	4.72	3.44	173,517	3.46
$3.75-$4.35	319,337	3.2	3.9	211,795	3.91
$4.69-$6.6	230,680	0.87	6.25	230,680	6.25
	3,991,468	4.31	$ 3.03	1,401,584	$ 3.28

d. Directors stock option plan:

In 1999, the Company adopted the 1999 Directors Stock Option Plan, and in 2008 shareholders approved an extension of the term of this plan through July 13, 2019. The original allotment of ordinary shares to this plan was 1,263,333. On December 15, 2006, the Company combined the remaining pool of options in the employee stock option plans reserve with the amount of options remaining in the Directors Stock Option Plan reserve.

Since the annual meeting of shareholders in 2003, new directors joining the Board are entitled to a grant of 50,000 options. Directors who are re-elected at the annual meeting of shareholders are entitled to additional grants of 16,667 options, though at the annual meeting held October 26, 2009 shareholders approved a one-time increase in the grants to re-elected directors to 30,000 options.

Each option granted under the Directors Stock Option Plan becomes exercisable at a rate of 1/16th of the shares every three months. Each option has an exercise price equal to the fair market value of the Ordinary shares on the grant date of such option. Until September 2005, each option granted had a maximum term of ten years, but since September 2005, the term of granted options is six years. Options will terminate earlier if the optionee ceases to be a member of the Board of Directors.

U.S. dollars in thousands, except share and per share data

NOTE 7: SHAREHOLDERS' EQUITY (Cont.)

On January 1, 2012, 1,047,827 options were outstanding under the Directors Stock Option Plan.
During 2012, the Company granted 166,669 options to Directors at a weighted average exercise price at $3.17 per share. The weighted average fair value of options granted during the year is $1.39. During the year, 37,209 options were exercised at a weighted average exercise price at $3.16 per share. As of December 31, 2012, 696,848 options were vested and unexercised and 1,131,885 were outstanding under the Directors Stock Option Plan.

e. Options to non-employees:

Issuance date	Options granted for Ordinary Shares	Exercise price per share	Options exercisable	Exercisable through
May 2006-2008	33,334	$ 3.21-$5.73	33,334	May 2013
February 16, 2012	53,000	$ 3.16	11,594	February 2016
	86,334		44,928	

The options vest and become exercisable at a rate of 1/16 of the options every three months. The Company has accounted for this grant under the fair value method of ASC 505-50. The fair value for these options was estimated using a Black-Scholes option-pricing model. Compensation expense for 2010, 2011 and 2012 amounted to $31, $0 and $11, respectively.

As of December 31, 2012, the Company had approximately $40 of unrecognized compensation expense related to non-vested stock options, expected to be recognized over a period of up to four years.

U.S. dollars in thousands, except share and per share data

NOTE 7: SHAREHOLDERS' EQUITY (Cont.)

g. Total stock-based compensation expenses recognized in 2010, 2011 and 2012:

The total stock-based compensation expense related to all of the Company's equity-based awards, recognized for the years ended December 31, 2010, 2011 and 2012, was comprised as follows:

	Year ended December 31,		
	2010	2011	2012
Cost of revenues	$ 38	$ 24	$ 51
Research and development	316	294	229
Selling and marketing	373	355	195
General and administrative	769	540	812
	$ 1,496	$ 1,213	$ 1,287

NOTE 8: INCOME TAXES

a. Corporate tax structure:

The Israeli corporate tax rate was 25% in 2010, 24% in 2011 and 25% in 2012 and onwards.

b. Tax benefits under Israel's Law for the Encouragement of Industry (Taxation), 1969:

The Company may currently qualify as an "industrial company" within the definition of the Law for the Encouragement of Industry (Taxation), as such, it may be eligible for certain tax benefits, including, inter alia, special depreciation rates for machinery, equipment and buildings, amortization of patents, certain other intangible property rights and deduction of share issuance expenses.

c. Net operating loss carryforwards:

As of December 31, 2012, the Company's net operating loss carryforwards for tax purposes amounted to approximately $70,008 (including capital loss carryforward of $15,659) which may be carried forward and offset against taxable income in the future, for an indefinite period.

As of December 31, 2012, for federal income tax purposes, the U.S. subsidiary had net operating loss carry-forwards of approximately $91,755 (including capital loss carryforwards of $1,700). These losses may offset any future U.S. taxable income of the U.S. subsidiary and will expire in the years 2012 through 2025.

U.S. dollars in thousands, except share and per share data

NOTE 8: INCOME TAXES (Cont.)

Utilization of U.S. net operating losses may be subject to substantial annual limitation due to the "change in ownership" provisions of the Internal Revenue Code of 1986 and similar state provisions. The annual limitations may result in the expiration of net operating losses before utilization.

Management currently believes that since the Company has a history of losses, and uncertainty with respect to future taxable income, it is more likely than not that some of the deferred tax assets regarding the loss carry forwards will not be utilized in the foreseeable future. Thus, a valuation allowance was provided to reduce deferred tax assets to their realizable value.

d. Deferred income taxes:

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. As of December 31, 2011 and 2012, the Company's deferred taxes were in respect of the following:

	December 31,	
	2011	2012
Deferred tax assets:		
Net operating loss carry-forwards	$ 50,234	$ 48,709
Capital loss carry-forwards	4,487	4,578
Reserves and allowances	192	183
Deferred revenues	244	188
Intangibles, Property and Equipment	116	76
Research and development costs	672	878
Deferred tax assets before valuation allowance	55,945	54,612
Valuation allowance	(51,060)	(49,025)
Deferred tax asset	$ 4,885	$ 5,587
Domestic:		
Current deferred tax asset, net	$ 1,572	$ 1,569
Non-current deferred tax asset, net	2,485	2,352
	4,057	3,921
Foreign:		
Current deferred tax asset, net	424	670
Non-current deferred tax asset, net	404	996
	828	1,666
	$ 4,885	$ 5,587
Deferred tax liabilities:		
Acquired intangibles	-	(3,187)
Deferred tax liabilities	$ -	$ (3,187)

U.S. dollars in thousands, except share and per share data

NOTE 8: INCOME TAXES (Cont.)

e. For the year ended December 31, 2010, the main reconciling items between the statutory tax rate of the Company and the effective tax rate are the non-recognition of the benefits from accumulated net operating loss carry forward due to the uncertainty of the realization of such tax benefits, as well as utilization of deferred tax asset of approximately $500 during 2010, offset by a recognition of a deferred tax asset of approximately $1,600 in respect of net operating loss carry-forwards and temporary differences that are more likely than not to be realized in the foreseeable future.

For the year ended December 31, 2011, the main reconciling items between the Company's statutory tax rate and the effective tax rate relates to changes in valuation allowance due to utilization of net operating loss carry forwards, recognition of net operating loss carry forward due to certainty of future realization of taxable income, and an increase in the Israeli tax rate (which resulted in an increase in the deferred tax asset), offset by increase in the exchange rate of the US dollars compared to the New Israeli Shekel.

For the year ended December 31, 2012, the main reconciling items between the Company's statutory tax rate and the effective tax rate relates to changes in valuation allowance due to utilization of net operating loss carry forwards, in the amount of $215 and a decrease in valuation allowance related to net operating losses expected to be realized in the foreseeable future, in the amount of $840.

f. Income before tax benefit consists of the following:

	Year ended December 31,		
	2010	2011	2012
Domestic	$ 3,124	$ 3,114	$ 1,430
Foreign	181	167	(570)
	$ 3,305	$ 3,281	$ 860

The Company is required to calculate and account for income taxes in each jurisdiction in which the Company or its subsidiary operate. Significant judgment is required in determining its worldwide provision for income taxes and recording the related assets and liabilities.

U.S. dollars in thousands, except share and per share data

NOTE 8: INCOME TAXES (Cont.)

Tax expense (benefit) is comprised of the following:

	Year ended December 31,		
	2010	2011	2012
Current taxes:			
Foreign	$ (2)	$ (2)	$ 124
Domestic	-	70	57
	$ (2)	$ 68	$ 181
Deferred taxes:			
Foreign	$ (270)	$ (357)	$ (942)
Domestic	(826)	(1,028)	136
	$ (1096)	$ (1,385)	$ (806)
	$ (1,098)	$ (1,317)	$ (625)

h. Tax assessments:

The Company has final tax assessments in Israel through 2006.

NOTE 9: GEOGRAPHIC INFORMATION

The Company conducts its business on the basis of one reportable segment. The Company has adopted ASC 280, “Segment Reporting”.

a. Revenues from external customers:

	Year ended December 31,		
	2010	2011	2012
Israel	$ 2,047	$ 2,044	$ 2,541
North America	9,184	12,655	11,847
Europe	4,454	4,869	5,737
Asia	1,976	3,036	3,484
Other	500	412	301
	$ 18,161	$ 23,016	$ 23,910

For the years ended December 31, 2010, 2011 and 2012, there are no major customers.

U.S. dollars in thousands, except share and per share data

NOTE 9: GEOGRAPHIC INFORMATION (Cont.)

b. The Company's net amount of long-lived assets is as follows:

	December 31	
	2011	2012
Israel	$ 246	$ 11,807
United States	4,144	3,807
Germany	-	462
Iceland	-	100
	$ 4,390	$ 16,176

NOTE 10: FINANCIAL INCOME (EXPENSES), NET

	Year ended December 31,		
	2010	2011	2012
Income:			
Interest on cash and cash equivalents and short term deposit	$ 20	$ 177	$ 144
Expenses:			
Foreign currency exchange differences and other	(75)	(204)	(64)
	$ (55)	$ (27)	$ 80

NOTE 11: SUBSEQUENT EVENTS

At about the time of the filing of this Annual Report, we were in the process of securing two credit lines from two Israeli banks in the total sum of up to $5,000. During 2012, we made significant investments (from our cash reserves) in the above described acquisitions of eleven and Frisk. In relation to these credit lines, the Company has agreed to grant security interests generally over all Company assets, and to refrain from encumbering its assets in favor of any other third parties. The Company anticipates that it will draw on these credit lines in the near future.

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Item 19. Exhibits.

The list of exhibits required by this Item is incorporated by reference to the Exhibit Index which precedes the exhibits to this Annual Report.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20–F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

COMMTOUCH SOFTWARE LTD.

By: /s/ Brian Briggs
Brian Briggs
Chief Financial Officer
April 25, 2013

Item 19. Exhibits

Exhibit Index

Exhibit Number	Description of Document
1.1	Memorandum of Association of the Company.(1)
1.2	Amended and Restated Articles of Association of the Company, as amended on December 15, 2011.(2)
4.1	Commtouch Software Ltd. 2006 U.S. Stock Option Plan.(3)
4.2	Amended and Restated Commtouch Software Ltd. 1999 Non–Employee Directors Stock Option Plan.(4)
4.3	Extension of Amended and Restated Commtouch Software Ltd. 1999 Non-Employee Directors Stock Option Plan.(5)
4.4	Commtouch Software Ltd. Amended and Restated Israeli Share Option Plan.(6)
4.5	Summary of Director Compensation.
4.6	Share Purchase Agreement of July 24, 2012 between Commtouch and former shareholders of Frisk.
4.7	Purchase and Assignment Agreement of November 15, 2012 between Commtouch and eleven.
4.8	Summary of two credit lines of April 2013.
8	List of Subsidiaries of the Company.
12.1	Certification of Company's Principal Executive Officer Pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a).
12.2	Certification of Company's Principal Financial Officer Pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a).
13	Certification of Company's Principal Executive Officer and Principal Financial Officer Pursuant to 18 U.S.C. 1350.
15	Consent of Kost, Forer, Gabbay & Kasierer, independent registered public accounting firm.
101	The following materials from our Annual Report on Form 20-F for the year ended December 31, 2012 formatted in XBRL (eXtensible Business Reporting Language) are furnished herewith: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Statements of Changes in Shareholders' Equity, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to Consolidated Financial Statements, tagged as blocks of text and in detail.

(1) Incorporated by reference to exhibits in Amendment No. 1 to Registration Statement on Form F–1 of Commtouch Software Ltd., File No. 333–78531. [filed June 3, 1999]

(2) Incorporated by reference to Exhibit 1.2 to Annual Report on form 20-F for the year ended December 31, 2012

(3) Incorporated by reference to Exhibit 99.4 to Registration Statement on Form S–8 No. 333–141177. [filed March 9, 2007]

(4) Incorporated by reference to Exhibit 99.1 to Registration Statement on Form S–8 No. 333–141177. [filed March 9, 2007]

(5) Incorporated by reference to Exhibit 4.6 to Annual Report on form 20-F for the year ended December 31, 2008.

(6) Incorporated by reference to Exhibit 99.3 to Registration Statement on Form S–8 No. 333–141177. [filed March 9, 2007]

Exhibit 4.5

SUMMARY OF DIRECTOR COMPENSATION

The following is a summary of the currently effective compensation of the non-employee directors of Commtouch Software Ltd. (the "Company") for services as directors:

- Directors are granted stock options, with new directors receiving an initial grant of 50,000 options and continuing directors receiving an "evergreen" option grant of 16,667 options. At the annual meeting in October 2009, shareholders approved a one-time increase of the evergreen option grant to 30,000 options.
- Through 2008, directors did not receive cash compensation for their services. However, at the annual meeting in December 2008, shareholders approved the payment of cash compensation, in addition to the stated options compensation, according to the following:

    1. NIS 31,700 base annually per director, as linked to the applicable Israeli consumer price index, payable in four equal installments at the beginning of each calendar quarter; and
    2. NIS 1,590 per director per face to face Board or committee meeting or NIS954 (60% of NIS 1590) in case of telephonic participation at such meeting, payable at the beginning of each calendar quarter following the quarter during which a Board member participated in a meeting. No separate per meeting compensation will be paid for committee meetings that are held on the same day immediately prior or subsequent to a Board meeting. In that event, a Board and committee meeting will be considered one meeting.
    3. For non-Israeli based directors, the amounts set forth will be paid in United States dollars, according to the representative rate of exchange published by the Bank of Israel on the date of payment.

Other than the foregoing option grants, cash compensation and reimbursement of expenses, the Company does not compensate its non-employee directors for serving on its board of directors.

Exhibit 4.6

EXECUTION VERSION

24 JULY 2012

SHARE PURCHASE AGREEMENT

BETWEEN

THE PERSONS LISTED IN SCHEDULE 1 AS SELLERS
(AS SELLERS)

AND

COMMTOUCH SOFTWARE LTD.
(AS BUYER)

RELATING TO SHARES IN

AN INCORPORATED ICELANDIC PRIVATE LIMITED COMPANY

TABLE OF CONTENTS

THIS AGREEMENT (hereinafter referred to as the "**Agreement**") is dated 24 July 2012

BETWEEN

(1) **THE PERSONS LISTED IN SCHEDULE 1** (hereinafter referred to as the "**Sellers**"); and

(2) **COMMTOUCH SOFTWARE LTD.**, a company incorporated and registered in the State of Israel having its registered address at 4A Hatzoran St. Netanya Israel 42504 (hereinafter referred to as the "**Buyer**").

Together the Sellers and the Buyer are hereinafter referred to as the "**Parties**" and each of them being a "**Party**".

BACKGROUND

(A) The Sellers, who are also the shareholders of the total share capital of FRISK (as defined below), shall cause FRISK to be divided pursuant to Article 107 (a) of the Act on Private Limited Companies No. 138/1994. The Division shall have entered into force prior to 11 September 2012 and certain assets and liabilities shall have been transferred to the Company, as the receiving company as a result of the Division, such assets and liabilities being detailed in Schedule 2.

(B) The Company shall have an issued share capital of ISK 52,000,000 divided into equal number of 1 ISK in nominal value.

(C) The Sellers have agreed to sell and the Buyer has agreed to buy the Shares (as defined below) subject to the terms and conditions of this Agreement.

AGREED TERMS

1. INTERPRETATION

1.1 The definitions and rules of interpretation in this clause 1 apply in this Agreement.

Assets: means the assets detailed in Schedule 2.

Business: means the business of FRISK, comprising the intellectual property, software, development, marketing, sales and support of anti-virus security products and associated services carried on by FRISK as at the date of this Agreement. The term Business shall not include the business of (i) intellectual property, software, development, marketing, sales and support of the Puki spell checker software and associated services, (ii) the genealogy database "'Íslendingabók", and (iii) real estate business.

Business Day: means a day (other than a Saturday, Sunday or public holiday) when banks in Iceland, Israel and the USA, are open for business.

Buyer's Group: means the Buyer and each of its subsidiaries, direct and indirect holding companies (including Commtouch Inc.) and any subsidiary of such holding companies.

Buyer's Lawyers: means LOGOS legal services, registration number 460100-2320, with its registered address at Efstaleiti 5, 103 Reykjavik, Iceland.

Claim: means a claim brought pursuant to the terms of this Agreement including any claims arising under the Warranties.

Commtouch Shares: means 750,000 restricted ordinary shares in the capital of the Buyer with a par value of Israeli New Shekel (NIS) 0.15 per share vesting in equal annual installments over a 4 year vesting cycle, commencing on the first anniversary of Completion.

Commtouch Inc.: means Commtouch Inc., a company incorporated and registered in California, USA having its registered address at 292 Gibraltar Drive, Suite 107, Sunnyvale, CA 94089, USA.

Company: means a private limited liability company to be incorporated as a result of the Division, to be named as FRISK Iceland ehf. and have its registered address at Þverholt 18, 105 Reykjavík, Iceland.

Completion: means the completion of the sale and purchase of the Shares in accordance with this Agreement.

Completion Date: has the meaning given in clause 5.2.

Completion Payment: means USD 1,200,000, or as set forth in the Side Letter.

Conditions: the conditions set out in Schedule 3.

Contracts: the contracts detailed in Schedule 2.

Control: means in relation to a body corporate, the power of a person or a consortium of persons to secure that the affairs of the body corporate are conducted in accordance with the wishes of that person or a consortium of persons:

(a) by means of the holding of shares, or the possession of voting power, in or in relation to that or any other body corporate; or

(b) by virtue of any powers conferred by the constitutional or corporate documents, or any other document, regulating that or any other body corporate;

and a **Change of Control** occurs if a person or a consortium of persons who control anybody corporate cease to do so or if another person or a consortium of persons acquires control of it.

Disclosed: means fairly, fully, clearly and accurately disclosed (with sufficient details to identify the nature and scope of the matter disclosed) in the Disclosure Letter.

Disclosure Letter: means the letter from the Sellers to the Buyer with the same date as this Agreement.

Division: means the division of FRISK pursuant to Article 107 (a) of the Act on Private Limited Companies No. 138/1994 which shall have entered into force prior to 11 September 2012, whereby the Company is the receiving company of the Assets and the Liabilities.

Due Diligence Documents: the documents that were provided by the Sellers to the Buyer pursuant to a list provided by the Sellers to the Buyer on the date hereof, copies of which have been made on the two identical cd-roms initialed by the

Parties at the date hereof of which one remains in the possession of the Sellers and the other remains in the possession of the Buyer.

Earn-out: means the earn-out mechanism, the terms of which are as set out in clause 4.5 and Schedule 6 hereto.

Earn-out Payments: has the meaning set out in paragraph 3.1 of Schedule 6.

Employees: the persons wholly employed by FRISK in the Business at the Completion Date (which, at the date of this Agreement, consists of those persons whose details are set out in the Employee List.

Employee List: means the list of employees from the Sellers to the Buyer with the same date as this Agreement and contained in the Disclosure Letter.

Encumbrance: means any interest or equity of any person (including any right to acquire, option or right of pre-emption or conversion) or any mortgage, charge, pledge, lien, assignment, hypothecation, security, interest, title, retention or any other security agreement or arrangement to create any of the above.

Escrow Agent: means Union Bank.

Escrow Agreement: means the escrow agreement, dated on or about the date hereof, between FRISK, Commtouch Inc., the Sellers, the Buyer and the Escrow Agent.

Escrow Account: means the bank account with the Escrow Agent with the details as set forth in the Escrow Agreement.

Escrow Amount: means the sum of USD 1,000,000, held by the Escrow Agent pursuant to the Escrow Agreement.

Escrow Expiry Date: means the date falling on the first anniversary of the IP Asset Transfer Agreement.

FRISK: means Friðrik Skúlason ehf. (also known as FRISK Software International), a private limited liability company organized and existing under the laws of Iceland, registered with the Icelandic Enterprise Register under the number 510693-2489, having its registered address at Þverholt 18, 105 Reykjavík, Iceland.

IP Assets: means all the intellectual property assets that are owned by FRISK or used or held for use by FRISK in the Business as currently conducted, including but not limited to the Rights which are transferred subject to the provisions of the IP Asset Transfer Agreement.

IP Asset Transfer Agreement: means the IP asset transfer agreement in the agreed form, to be entered into immediately prior to Completion between FRISK and Commtouch Inc., in respect to the sale and purchase of the IP Assets.

Lease Agreement: means the lease agreement in the agreed form, to be entered into on, or immediately prior to Completion, between the Company (as the lessee) and FRISK (as the lessor), in respect to the real estate at Þverholt 18, 105 Reykjavík, Iceland.

Liabilities: means the liabilities detailed in Schedule 2.

Purchase Price: means the purchase price for the Shares to be paid by the Buyer to the Sellers in accordance with clause 4.

Sellers Account: means the bank account with the Sellers' Lawyers, with the following details:

IBAN: IS81 0303 3810 6309 2704 6352 59
SWIFT: ESJAISRE
Bank: Arion bank hf.
Address: Laugavegur 120, 105 Reykjavík, Iceland
Name of account: Björg M. Ólafsdóttir, ID no. 270463-5259

Sellers' Lawyers: means Jonsson & Hall Law Firm, registration number 671291-3289, with its registered address at Sudurlandsbraut 4, 108 Reykjavik, Iceland.

Shares: means 52,000,000 shares of a nominal value of 1 ISK each in the Company, representing 100% of the Company's issued share capital immediately following the Division, all of which shall have been fully paid for.

Share Subscription Letter: a letter from the Sellers to the Buyer, in the agreed form, to be entered into immediately prior to Completion, setting out the terms and conditions for the issue of the Commtouch Shares.

Side Letter: means the side letter entered into by the Buyer and the Sellers on the date hereof.

Substantiated Claim: means a Claim which has been validly made in accordance with this Agreement and in respect of which liability is (1) agreed in writing between the Sellers and the Buyer; or (2) adjudicated on by a court of competent jurisdiction and no right of appeal lies in respect of such adjudication, or the Parties are debarred by passage of time or otherwise from making an appeal.

Tax or Taxation: means all forms of tax or taxation including, in particular, any charge, tax, duty, levy, impost, withholding or liability wherever chargeable imposed for support of national, state, federal, municipal or local government or any other person in any jurisdiction and any penalty, fine, surcharge, interest, charges or costs payable in connection with any such tax or taxation.

Third Party Consent: a consent, licence, approval, authorisation or waiver required from a third party for the conveyance, transfer, assignment or novation in favour of the Buyer of any of the Contracts on terms acceptable to the Buyer.

Transaction: means the transaction contemplated by this Agreement and the IP Asset Transfer Agreement or any part of that transaction.

Warranties: means the warranties in Schedule 5 hereto.

Working Capital: means trade debtors, cash, stock, and other debtors, prepayments and accrued income less its trade and other creditors and its unpaid and accrued liabilities and expenses (including but not limited to unpaid taxation).

1.2 Clause and schedule headings do not affect the interpretation of this Agreement.

1.3 A person includes a corporate or unincorporated body.

1.4 Words in the singular include the plural and in the plural include the singular.

1.5 A reference to a law is a reference to it as it is in force for the time being taking account of any amendment, extension, application or re-enactment and includes any subordinate legislation for the time being in force made under it.

1.6 Warranties given "so far as the Sellers are aware" or any similar provision, are deemed to be given to the best of the knowledge, information and belief of the Sellers after they have made all reasonable and careful enquiries and shall be deemed to include that which can reasonably be expected that they would be aware of, in their current or former capacity as employees, shareholders and/or directors of the Company and/or FRISK.

1.7 In the event any action or event described herein is set to occur on a day that is not a Business Day, such action or event shall instead occur on the immediately following Business Day.

1.8 Documents in agreed form are documents in the form agreed by the Parties to this Agreement and initialed by them for identification.

1.9 Unless otherwise expressly provided, the obligations and liabilities of the Sellers under this Agreement are joint and several.

2. CONDITIONS

2.1 Completion of this Agreement is subject to the Conditions in Schedule 3 being satisfied or waived by the date and time provided in clause 2.4.

2.2 If any of the Conditions are not satisfied or waived by the date and time referred to in clause 2.4, this Agreement shall cease to have effect immediately after that date and time except for any rights or liabilities that have accrued under this Agreement.

2.3 The following provisions shall continue to have effect, notwithstanding failure to waive or satisfy the Conditions:

(a) clause 1;

(b) clause 2.2 and this clause 2.3;

(c) clause 11;

(d) clause 12;

(e) clause 14;

(f) clause 15; and

(g) clause 20.

2.4 The Sellers and the Buyer shall use all reasonable endeavours (so far as lies within their respective powers) to procure that the Conditions are satisfied as soon as practicable and in any event no later than 14 September 2012 or at such later time and date as may be agreed in writing by the Sellers and the Buyer.

2.5 The Buyer and the Sellers shall co-operate fully in all actions necessary to procure the satisfaction of the Conditions including, but not limited to, the provision by all parties of all information reasonably necessary to make any notification or filing that the Buyer deems to be necessary or as requested by any relevant authority, keeping all parties informed of the progress of any notification or filing and providing such assistance as may reasonably be required.

2.6 The Buyer may, to such extent as it thinks fit and is legally entitled to do so, waive the conditions set out in the Conditions by written notice to the Sellers.

3. SALE AND PURCHASE

3.1 On the terms of this Agreement the Sellers shall sell, and the Buyer shall buy (with effect from Completion), the Shares.

3.2 Each Seller:

(a) has, or shall on Completion have, full authority to sell its part of the Shares under the terms set out in this Agreement;

(b) shall at its own cost give the Buyer the full legal and beneficial title to the Shares; and

(c) sells the Shares free from all Encumbrances.

3.3 The Sellers confirm to the Buyer that the Company has no outstanding debt of any kind.

3.4 The Sellers hereby irrevocably and unconditionally waive all rights of pre-emption or other restriction on transfer of the Shares conferred on them by either the articles of association of the Company or in any other way.

3.5 The Shares are sold with full title guarantee and all rights that attach, or may in the future attach, to them (including, in particular, the right to receive all dividends and distributions declared, made or paid on or after the date of this Agreement).

3.6 The Buyer is not obliged to complete the purchase of any of the Shares unless the purchase of all the Shares and the IP Assets is completed simultaneously, or the purchase of the IP Assets is completed immediately before Completion.

4. PURCHASE PRICE

4.1 The Purchase Price shall consist of (1) the Completion Payment; (2) the Commtouch Shares; (3) the Earn-out Payments, and (4) less the amount paid in respect of any Substantiated Claims.

4.2 The Completion Payment shall be paid by the Buyer in USD in cash to the Sellers on Completion into the Sellers Account, or as set forth in the Side Letter.

4.3 The Commtouch Shares shall be delivered to the Sellers by transferring the Commtouch Shares in accordance with the provisions of the Share Subscription Letter.

4.4 Subject to and in accordance with the provisions set forth in Schedule 6, the Buyer shall pay to the Sellers the Earn-out Payments.

4.5 The Purchase Price shall be adjusted as set out in Schedule 7.

5. COMPLETION AND TERMINATION

5.1 Completion shall take place on the Completion Date:

(a) at the offices of the Buyer's Lawyers at Efstaleiti 5, 103 Reykjavík, Iceland; or

(b) at any other place or time as agreed in writing by the Sellers and the Buyer.

5.2 **Completion Date** means 14 September 2011, but subject to clause 5.9 and clause 2.4, if the Conditions have not been satisfied or waived in accordance with clause 2 on or before that date, means:

(a) the fifth Business Day after the Conditions are satisfied or waived;

(b) any other date agreed in writing by the Sellers and the Buyer; or

(c) the date to which Completion is deferred in accordance with clause 5.6.

5.3 The Sellers undertake to the Buyer that the Business shall be conducted in the manner provided in Part 1 of Schedule 4 from the date of this Agreement until Completion and give the Buyer the undertakings set out in that Schedule.

5.4 At, or immediately prior to, Completion the Sellers shall:

(a) deliver or cause to be delivered the documents and evidence set out in Part 2 of Schedule 4; and

(b) deliver any other documents referred to in this Agreement as being required to be delivered by them; and

(c) cause completion under the IP Asset Transfer Agreement.

5.5 At Completion the Buyer shall pay the Completion Payment to the Sellers (or as set forth in the Side Letter) and procure the delivery of the countersigned Share Subscription Letter to the Sellers.

5.6 If the Sellers do not comply with clause 5.4 in any material respect, the Buyer may, without prejudice to any other rights it has:

(a) proceed to Completion; or

(b) defer Completion to a date no more than 28 days after the date on which Completion would otherwise have taken place; or

(c) rescind this Agreement.

5.7 If Completion does not take place because of the Sellers non-fulfilment or failure to perform any of its obligations under clause 5.4, which is within their control, or to fulfil any of the Conditions (including in respect of the Division), to the extent that it is within their control, the Sellers shall pay the Buyer the sum of USD 200,000 by way of compensation for all costs and expenses incurred by the Buyer's Group in the negotiation, preparation and performance of this Agreement and the Asset Sale Agreement, including but not limited to the cost of legal and financial advisers. For the avoidance of doubt, this clause does not limit the amount that the Buyer may claim under this Agreement in the event of the above occurring.

The same compensation duty, of the same amount, applicability and limitations, applies to the Buyer, should Completion not take place because of the Buyer's non-fulfilment or failure to perform any of its obligations under clause 5.5, which is within its control, or to fulfil any of the Conditions, to the extent that it is within its control.

5.8 As soon as possible after Completion the Sellers shall send to the Buyer all records, correspondence, documents, files, memoranda and other papers relating to the Company and the Business not required to be delivered at Completion to the extent such records, correspondence, documents, files, memoranda and other papers relating to the Company and the Business are in the possession of and/or known by the Sellers to exist.

5.9 This Agreement may be terminated, and the Transaction abandoned, at any time prior to Completion:

(a) by the mutual written consent of the Sellers and the Buyer;

(b) by the Buyer if Completion has not occurred by 14 September 2012; or

(c) by the Buyer, upon a breach of any representation, warranty, covenant or agreement on the part of any of the Sellers set forth in this Agreement, or if any representation or warranty of the Sellers shall have become untrue.

5.10 The right to terminate this Agreement pursuant to clause 5.9 above shall not be available to any party whose action or failure to act has been a principal cause of or resulted in the failure of Completion to occur on or before such date.

6. WARRANTIES

6.1 The Buyer enters into this Agreement on the basis of, and in reliance on, the Warranties given by the Sellers and set out in Schedule 5.

6.2 The Sellers warrant and represent to the Buyer that, except as Disclosed, each Warranty is true, correct and not misleading on the date of this Agreement and on the Completion Date.

6.3 Without prejudice to the right of the Buyer to claim on any other basis or take advantage of any other remedies available to it, the Sellers agree and shall procure that the Buyer is entitled to deduct the amount of any Substantiated Claim from (i) the Escrow Amount (provided such claim arises no later than on the Escrow Expiry Date), (ii) the Earn-out Payments and/or (iii) any unvested Commtouch Shares.

6.4 The Buyer may postpone payments of the Earn-Out Payments and unvested Commtouch Shares, provided that it notifies the Sellers in writing that it has a Claim (containing a summary of the subject matter and amount of such claim and of the circumstances relating to such claim). Such payments shall be made to the Sellers if legal proceedings have not been issued and validly served in respect of the Claim concerned within 6 months of receipt by the Sellers of written notice of such claim. To the extent that such a claim does not become a Substantiated Claim, the Buyer shall make a payment to the Sellers of the payment that was postponed.

6.5 The basis of damages for any Claim shall be the amount necessary to put the Company and the Buyer in the position it would have been if the covenant or Warranty had not been breached and had been true, correct and not misleading.

6.6 The Sellers undertake to pay to the Buyer any amounts in respect to Substantiated Claims, although never succeeding the Purchase Price (less any amounts that the Buyer receives from the Escrow Amount).

6.7 The Buyer is not entitled to recover damages or otherwise obtain restitution more than once in respect of the same loss.

6.8 If at any time within the period of 1 year beginning with the Completion Date, any Seller becomes aware that a Warranty has been breached, is untrue or is misleading, or has a reasonable expectation that any of those things might occur, it must immediately:

(a) notify the Buyer in sufficient detail to enable the Buyer to make an accurate assessment of the situation; and

(b) if requested by the Buyer, use its reasonable endeavours to prevent or remedy the notified occurrence.

6.9 Each of the Warranties is separate and, unless specifically provided, is not limited by reference to any other Warranty or anything in this Agreement.

6.10 No information of which the Buyer and/or its agents and/or advisers has knowledge (actual, constructive or imputed), or which could have been discovered (whether by investigation made by the Buyer or made on its behalf), shall prejudice or prevent any Claim or reduce any amount recoverable thereunder.

7. LIMITATIONS ON CLAIMS

7.1 This clause limits the liability of the Sellers in relation to any Claim pursuant to clause 6 and Schedule 5 (a "**Warranty Claim**").

7.2 The liability of the Sellers for all Warranty Claims that become Substantiated Claims when taken together shall be limited to the Purchase Price plus an amount in respect of reasonable legal costs incurred by the Buyer in Iceland in bringing any such Substantiated Claims, such legal costs not to exceed ISK 2,500,000.

7.3 The Sellers are not liable for a Warranty Claim unless the Buyer has given the Sellers notice in writing of the Warranty Claim, summarising the nature of the Warranty Claim as far as it is known to the Buyer and the amount claimed, within the period of 2 years beginning with the Completion Date, provided however that such notice period will instead be a 6 year notice period with respect to any Warranty Claim relating to the tax warranties in paragraph 25 of Schedule 5.

7.4 The Sellers are not liable for any Warranty Claim to the extent that the Warranty Claim relates to matters Disclosed.

7.5 Nothing in this clause 7 applies to a claim that arises or is delayed as a result of dishonesty, fraud, wilful misconduct or wilful concealment by the Sellers, their agents or advisers.

7.6 Nothing in this clause 7 applies to a claim that relates to the Warranties in paragraphs 1 and 2 of Schedule 5.

8. INDEMNITIES OF THE SELLERS

8.1 The Sellers undertake to indemnify, and to keep indemnified, the Buyer and the Company against all losses or liabilities which may be actually suffered or incurred by any of them and which arise directly or indirectly in connection with:

(a) the Sellers' breach of a Warranty (including, without limitation, any Warranty proving to be untrue, misleading or false) or their non-fulfillment of or failure to perform any covenant or agreement required of them pursuant to this Agreement;

(b) the Division, including if a claim is brought against the Company pursuant to Article 107 (a) (3) of the Act on Private Limited Companies No. 138/1994 or if any Asset, Liability or Contract has not been effectively transferred to the Company by Completion;

(c) FRISK's breach of any Warranty (including, without limitation, any Warranty proving to be untrue, misleading or false) or its non-fulfillment of or failure to perform any covenant or agreement required of it pursuant to the IP Asset Transfer Agreement;

(d) the employment of the Employees or the termination of their employment by the Company or FRISK prior to the Completion Date or as a result of the Division;

(e) any failure by the Company or FRISK before the Completion Date to comply with its legal obligations in respect of any of the Employees;

(f) the transfer to the Company or Commtouch Inc. of the employment of any employee of FRISK other than the Employees;

(g) any claims under any guarantees or warranties given by the Sellers to any customer in relation to goods sold or services rendered by the Sellers before the Completion Date, the liability for which shall remain absolutely with the Sellers; or

(h) any claims relating to and payable in respect of the Business which are attributable to the period up to and including the Completion Date, including any act or omission on the part of the Sellers in relation to the Contracts or any defects in, or alleged defects in, goods supplied or services provided prior to the Completion Date.

8.2 The Parties acknowledge that the Act on the legal status of employees due to a change of control of companies' No. 72/2002 is applicable to the Transaction. Sellers undertake to indemnify, and to keep indemnified, the Buyer and the Company against all losses or liabilities which may be actually suffered or incurred by any of them and which arise directly or indirectly in connection with any claims of previous and current employees of FRISK relating to a period prior than the Completion Date. Notwithstanding the above, the Sellers are not liable for accrued but unpaid holidays of employees. The Sellers represent and warrant that the amount of accrued but unpaid holidays of employees is correctly stipulated in a document which they delivered to the Buyer.

8.3 The Sellers are jointly and severally liable for the obligations of FRISK under the IP Asset Transfer Agreement. Commtouch Inc. may rely on the indemnity provided by the Sellers under this paragraph. For the avoidance of doubt, should the Buyer or Commtouch Inc. have a claim against the Sellers, such a claim shall be brought before Icelandic courts, or such other courts whereby the Sellers are domiciled at each time.

8.4 Any payment made in respect of a claim under this clause 8 shall include:

(a) an amount in respect of all costs and expenses incurred by the Buyer or the Company or any of the Buyer's Group in relation to the bringing of the claim (including a reasonable amount in respect of management time); and

(b) any amount necessary to ensure that, after any Taxation of the payment, the Buyer is left with the same amount it would have had if the payment was not subject to Taxation.

9. CONTRACTS

Between the date of this Agreement and the Completion Date, the Sellers shall procure from the counterparties to the Contracts their consent to the assignment of the Contracts and/or waiver of any change of control or other termination rights

which arise or are likely to arise as a result of the Division or the Transaction ("**the Contract Consents**").

10. RESTRICTIONS ON THE SELLERS

10.1 Each of the Sellers severally covenants with the Buyer that he shall not:

(a) at any time during the period of 2 years beginning with the Completion Date, in any geographic areas in which the Business was carried on at the Completion Date, carry on or be employed, engaged or interested in any business which would be in competition with any part of the Business as the Business was carried on at the Completion Date; or

(b) at any time during the period of 2 years beginning with the Completion Date, deal with any person who is, at the Completion Date, or who has been at any time during the period of 12 months immediately preceding that date, a client or customer of either FRISK in respect of the Business or the Company; or

(c) at any time during the period of 2 years beginning with the Completion Date, canvass, solicit or otherwise seek the custom of any person who is, at the Completion Date, or who has been at any time during the period of 12 months immediately preceding that date, a client or customer of either FRISK in respect of the Business or the Company; or

(d) at any time during the period of 2 years beginning with the Completion Date:

(i) offer employment to, enter into a contract for the services of, or attempt to entice away from the Company, any individual who is at the time of the offer or attempt, and was at the Completion Date, employed or directly or indirectly engaged in an executive or managerial position in the Business; or

(ii) procure or facilitate the making of any such offer or attempt by any other person; or

(e) at any time after Completion, use in the course of any business:

(ii) any trade or service mark, business or domain name, design or logo which, at Completion, was or had been used in respect of the Business; or

(iii) anything which is, in the reasonable opinion of the Buyer, capable of confusion with such words, mark, name, design or logo; or

(f) at any time during a period of 2 years beginning with the Completion Date, solicit or entice away from the Business any supplier who had supplied goods or services to the Company or FRISK in respect of the Business at any time during the period of 12 months immediately preceding the Completion Date, if that solicitation or enticement causes or would cause

such supplier to cease supplying, or materially reduce its supply of, those goods or services to the Company or any member of the Buyer's Group.

10.2 Nothing in this clause 10 prevents the Sellers or any of them from holding for investment purposes only:

(a) any units of UCITS or investment funds within the meaning of the Act on UCITS, investment funds and professional investment funds No. 128/2011; or

(b) not more than 5% of any class of shares or securities of any company traded on any stock exchange in any geographic areas in which any business of the Company or any of the Subsidiaries was carried on at the Completion Date; or

(c) any of the Sellers´ existing investments in Iceland at the date hereof.

10.3 Each of the covenants in this clause 10 is a separate undertaking by each Seller in relation to himself and herself and his or her interests shall be enforceable by the Buyer separately and independently of its right to enforce any one or more of the other covenants contained in this clause 10. Each of the covenants in this clause 10 is considered fair and reasonable by the parties. If any restriction is found to be unenforceable, but would be valid if any part of it were deleted or the period or area of application reduced, the restriction shall apply with such modifications as may be necessary to make it valid and enforceable.

10.4 In the event of any breach of any of the covenants in this clause 10 the Sellers shall on demand pay to the Buyer the sum of USD 200,000. For the avoidance of doubt, this clause does not limit the amount that the Buyer may claim under this Agreement in the event of a breach of any of the covenants in this clause 10.

11. CONFIDENTIALITY AND ANNOUNCEMENTS

11.1 Each of the Parties agree that the content of this Agreement as well as any and all information being delivered or disclosed (whether orally or in writing) to the other party in connection herewith shall be deemed to be confidential.

11.2 The Parties have on the date of this Agreement agreed a text of a joint press release to announce the Transaction which shall be announced on said date or, if not reasonably possible, the next business day thereafter.

11.3 This clause 11 shall survive the termination of this Agreement and is subject to any requirements of the Buyer under applicable law and/or the rules of the Nasdaq Stock Market and the US Securities Exchange Commission.

12. WHOLE AGREEMENT

12.1 This Agreement, and any documents referred to in it, constitute the whole agreement between the Parties and supersede any arrangements, understandings or previous agreements between them relating to the subject matter they cover.

13. VARIATION AND WAIVER

13.1 Any variation of this Agreement shall be in writing and signed by or on behalf of all Parties.

13.2 Any waiver of any right under this Agreement is only effective if it is in writing, and it applies only in the circumstances for which it is given and shall not prevent the Party who has given the waiver from subsequently relying on the provision it has waived.

13.3 No failure to exercise or delay in exercising any right or remedy provided under this Agreement or by law constitutes a waiver of such right or remedy or will prevent any future exercise in whole or in part thereof.

13.4 No single or partial exercise of any right or remedy under this Agreement shall preclude or restrict the further exercise of any such right or remedy.

13.5 Unless specifically provided otherwise, rights arising under this Agreement are cumulative and do not exclude rights provided by law.

14. COSTS

14.1 Unless otherwise provided, all costs in connection with the negotiation, preparation, execution and performance of this Agreement, and any documents referred to in it, shall be borne by the Party that incurred the costs.

15. NOTICE

15.1 A notice given under this Agreement:

(a) shall be in writing in the English language;

(b) shall be sent for the attention of the person, and to the address, or fax number, given in this clause 15 (or such other address, fax number or person as the party may notify to the others in accordance with the provisions of this clause 15); and

(c) shall be:

(i) delivered personally; or

(ii) sent by fax; or

(iii) sent by pre-paid first class post, recorded delivery or registered post; or

(iv) by email.

15.2 The addresses for service of notice are:

On behalf of the Sellers:

(i) name: Friðrik Skúlason.

(ii) address: Stigahlíð 65, 105 Reykjavík, Iceland

(iii) for the attention of: Friðrik Skúlason / Björg M. Ólafsdóttir

(iv) with a copy to: the Sellers Lawyers

c/o Einar Þór Sverrisson, hrl.

einar@law.is

fax: +354 414 4101

The Buyer:

(i) name: Commtouch Software Ltd.

(ii) address: 4A Hatzoran St., Netanya 42504 Israel

(iii) fax: 972-9-8636863

(iv) for the attention of: General Counsel

(v) with a copy to: the Buyer's Lawyers

c/o Benedikt Egill Árnason, hdl.

benedikt@logos.is

fax: +354 5400 301

15.3 To prove service it is sufficient to prove that the notice was transmitted by fax to the fax number of the party or, in the case of post, that the envelope containing the notice was properly addressed and posted, or in the case of email, that no delivery failure notification was received.

16. FURTHER ASSURANCE

16.1 The Parties shall (at their expense) promptly execute and deliver all such documents, and do all such things, as the other Party may require from time to time for the purpose of giving full effect to the provisions of this Agreement.

17. COUNTERPARTS

17.1 This Agreement may be executed in any number of counterparts, each of which is an original and which together have the same effect as if each party had signed the same document.

18. SEVERANCE

18.1 If any provision of this Agreement (or part of a provision) is found by any court or administrative body of competent jurisdiction to be invalid, unenforceable or illegal, the other provisions shall remain in force.

18.2 If any invalid, unenforceable or illegal provision would be valid, enforceable or legal if some part of it were deleted, the provision shall apply with whatever modification is necessary to give effect to the commercial intention of the Parties.

19. ASSIGNMENT

19.1 Except as provided otherwise, the Sellers shall not assign, or grant any Encumbrance or security interest over, any of its rights under this Agreement or any document referred to in it without the prior written consent of the Buyer.

19.2 The Buyer may assign its rights and obligations under this Agreement (or any document referred to in the Agreement) to a member of the Buyer's Group.

19.3 If there is an assignment pursuant to clause 19.1 or 19.2:

(a) the Sellers shall not discharge their obligations under this Agreement to the assignor until it receives notice of the assignment;

(b) the assignee may enforce this Agreement as if it were a party to it; and

(c) the liability of the Sellers to any assignee cannot be greater than its liability to the Buyer.

20. GOVERNING LAW AND JURISDICTION

20.1 This Agreement and any disputes or claims arising out of or in connection with its subject matter are governed by and construed in accordance with the law of Iceland.

20.2 The Parties irrevocably agree that the courts of Iceland have exclusive jurisdiction to settle any dispute or claim that arises out of or in connection with this Agreement or its subject matter or formation (including non-contractual disputes or claims).

20.3 This Agreement is in English language, in the case of conflict with translations the English text shall prevail. This Agreement has been entered into on the date stated at the beginning of it.

SCHEDULE 1 PARTICULARS OF THE SELLERS

	Name	Identification number	Shares held	Completion Payment	Bank account	Portion of Commtouch Shares
1.	Friðrik Skúlason		26,000,000	US$ 600,000*	Sellers Account	50%
2.	Björg Marta Ólafsdóttir		26,000,000	US$ 600,000*	Sellers Account	50%
	Total		**52,000,000 (100%)**	**US$ 1,200,000* (100%) *or as set forth in the Side Letter**		**750,000 (100%)**

SCHEDULE 2 Assets and Liabilities

A. Assets

All assets of FRISK (including receivables)shall be the property of the Company, other than the following assets:

1. The property at Þverholt 18. Registration number, 201-1215 (05 0101) and 201-1216 (06 0101).
2. The domain “complex.is”.
3. Genealogy:
    a. Genealogy library (collection of books, manuscripts, microfiches and other information related to genealogy.
    b. All software related to genealogy, in particular the program Espólín, and the Islendingabok project. This includes software rights, source code, object code, manuals, (in electronic or paper form).
    c. All available data on existing customers of the genealogy program.
    d. The domain “islendingabok.is.
4. Icelandic spelling checker:
    a. Any software directly related to the development of the spelling checker (Púki), the grammar checker or related projects.
    b. Manuals, CDs and any marketing material directly associated with those projects.
    c. Any software related to the “Vefpúki” project.
    d. Assorted books (mostly dictionaries or books on Icelandic grammar) purchased for the development of those projects.
    e. Collections of words and texts, collected for the benefit of those projects, in particular texts received from Morgunblaðið.
    f. All available data on customers of the spelling checker.
    g. The domain “puki.is”.
5. Any other rights that relate to the property, the domain “complex.is”, genealogy, the Icelandic spelling checker and intellectual property.

For the avoidance of doubt, the IP Assets will be the property of Commtouch Inc. at the Completion Date.

B. Liabilities

Liabilities relating to the normal operation of FRISK, which will not remain at FRISK subsequent to the Division, are as follows but will be fully paid by FRISK until the Completion Date:

1. Liabilities relating to employees
    a. Salaries
    b. Accident Insurance
    c. Pension Fund Contributions
    d. Withholding Tax Obligations
        i. Income Tax
        ii. Social Security Tax
    e. Car Allowance
    f. Union Fees

2. Liabilities relating to Production Cost
3. Liabilities relating to Lease Payments for Þverholt 18, 105 Reykjavík
4. Liabilities relating to Operation Cost
    a. Advertising
        i. Internet
        ii. Upload/Payperd/Sigma/CDN
        iii. Printing
    b. Telephone and Internet Access
    c. ISNIC fees
    d. Domain fees
    e. Verisign fees
    f. Fees for VeriCe/Akamai/Hostway hosting
    g. Specialist services
    h. Software Fees
    i. Computer Maintenance
    j. Product Deliver
    k. Security system for the offices at Þverholt 18, 105 Reykjavík
    l. Debt collecting, INTRUM
    m. Legal and Accounting fees
    n. Cleaning for the offices at Þverholt 18, 105 Reykjavík
    o. Service-fees to credit card companies

C. Contracts

SCHEDULE 3 Conditions

1. That the Division has entered into force on or before 11 September 2012.

2. That all the Contract Consents in respect of the Contracts have been obtained to the satisfaction of the Buyer.

3. That the IP Asset Transfer Agreement has been entered into and duly executed by FRISK and Commtouch Inc., and completed.

4. That the Central Bank of Iceland has granted an exemption as requested in the exemption request signed by LOGOS legal services and Jonsson & Hall Law Firm.

5. That the Company has entered into employment agreements with the employees that are detailed in the Disclosure Letter, in the form and substance acceptable to the Buyer.

6. That the Employees have executed a declaration in the agreed form confirming that any intellectual property created by them in the course of their employment by FRISK (prior to the Division) and by the Company (following the Division) shall be the property of the Company (the "**Employee IP Letters**").

7. That the Company has entered into the Lease Agreement.

8. Each of the representations and warranties contained in this Agreement and in the IP Asset Transfer Agreement shall be true and correct as of the date hereof and as of the Completion Date as though made on and as of the Completion Date (except for those representations and warranties which address matters only as of a particular date, which need only be true and correct as of such date).

9. No person:

    (i) having commenced, or threatened to commence, any proceedings or investigation for the purpose of prohibiting or otherwise challenging or interfering with the Transaction or the Division; or

    (ii) having taken or threatened to take any action as a result of, or in anticipation of, the Transaction or the Division, that would be materially inconsistent with any of the Warranties; or

    (iii) having enacted or proposed any legislation or regulation which would prohibit, materially restrict or materially delay the implementation of the Transaction, the Division or the operations of the Company or FRISK; or

    (iv) having made a claim against FRISK and/or the Company which has not been fairly, fully, clearly and accurately disclosed in the Due Diligence Documentation.

10. That there has been no material adverse change in the business, operations, assets, position (financial, trading or otherwise), profits or prospects of FRISK or the Business, taken as a whole, or any event or circumstance that may result in such a material adverse change.

SCHEDULE 4 Completion

Part 1. Conduct between execution and Completion

1. The Sellers shall procure that the Business shall be conducted in the manner provided in this Part 1 of this Schedule 4 from the date of this Agreement to Completion.

2. The Sellers shall procure that the Business shall be carried on in the normal course.

3. The Sellers shall procure that neither the Company nor FRISK in respect of the Business shall:

   (i) dispose of any of the Assets or material assets used or required for the operation of the Business; or

   (ii) allot or agree to allot any shares or other securities or repurchase, redeem or agree to repurchase or redeem any of the shares; or

   (iii) pass any resolution; or

   (iv) enter into, modify or agree to terminate any Contract (as defined in paragraph 11 of Schedule 5); or

   (v) modify, terminate or make any material amendments in respect to the Contracts other than in the ordinary course of business; or

   (vi) incur any capital expenditure in excess of USD 10,000; or

   (vii) borrow any sum in excess of USD 10,000; or

   (viii) enter into any lease, lease-hire or hire-purchase agreement or agreement for payment on deferred terms; or

   (ix) pay any dividend or make any other distribution of its assets; or

   (x) make, or agree to make, material alterations to the terms of employment (including benefits) of any of its directors or employees; or

   (xi) provide or agree to provide any non-contractual benefit to any director, employee or their dependants; or

   (xii) dismiss any of its employees or employ or engage (or offer to employ or engage) any person; or

   (xiii) create any Encumbrance over any of its assets or its undertaking; or

   (xiv) institute, settle or agree to settle any legal proceedings relating to its business, except debt collection in the normal course of business; or

   (xv) grant, modify, agree to terminate or permit the lapse of any intellectual property rights or enter into any agreement relating to any such rights; or

   (xvi) pay any management charge to the Sellers or FRISK or any of their connected parties; or

(xvii) incur any liability to the Sellers or FRISK or any of their connected parties, other than trading liabilities incurred in the normal course of business; or

(xviii) do anything in respect of the Liabilities other than make payments in respect of the Liabilities in the ordinary course of business; or

(xix) vary the terms on any lease agreements; or

(xx) make any material change to the accounting procedures or principles by reference to which its accounts are drawn up; or

(xxi) waive, release, assign, settle or compromise any claim, suit, action or proceeding; or

(xxii) enter into any agreement containing any non-competition, "most favoured nations" or exclusivity restrictions; or

(xxiii) enter into any agreement containing any exclusivity restrictions.

11. The Company and FRISK may do anything falling within paragraph 3 of Part 1 of this Schedule 4 if:

(a) the Buyer has given prior written consent; or

(b) required to effect the Division; or

(c) required to effect completion of the IP Asset Transfer Agreement.

12. The Sellers shall use their best endeavours to maintain the trade and trade connections of the Company and FRISK.

13. The Sellers shall give to the Buyer as soon as possible full details of any material change in the business, financial position or assets of the Company and/or FRISK.

Part 2. What the Sellers shall deliver and evidence to the Buyer at Completion

At Completion, the Sellers shall deliver to the Buyer, or cause to be delivered:

1. a share register executed by the board of directors of the Company, evidencing the transfer of the Shares from the Sellers to the Buyer, free from any Encumbrances;
2. the executed Escrow Agreement;
3. the executed IP Asset Transfer Agreement;
4. the executed Lease Agreement;
5. the executed Share Subscription Letter;

6. the executed Employee IP Letters for each Employee;
7. the executed Contracts Consents; and
8. any other ancillary documents required under or in connection with this Agreement.

SCHEDULE 5 Warranties

1. POWER TO SELL THE COMPANY

1.1 Each of the Sellers has the necessary power and authority to enter into and perform this Agreement and the other documents referred to in it.

1.2 This Agreement and the other documents referred to in it constitute (or shall constitute when executed) valid, legal and binding obligations on the Sellers in the terms of the Agreement and the documents.

2. SHARES IN THE COMPANY AND THE ASSETS AND LIABILITIES

2.1 The Shares constitute 100% of the issued share capital of the Company and are fully paid, and no other rights to an issuance of unissued Shares are vested in any third party.

2.2 The Company is formed as a result of the Division and has no liabilities other than the Liabilities and pursuant to Article 107 (a) (3) of the Act on Private Limited Companies No. 138/1994.

2.3 No dividends or distributions shall be declared, made or paid by the Company or FRISK in respect of any period prior to the Completion Date.

2.4 The Company has not made any dividend or distribution, whether by cash or otherwise, to its shareholders.

2.5 The particulars of Schedule 2 are true, correct and not misleading.

2.6 As at Completion, the Company shall be a party to the Contracts.

2.7 There are no other assets, liabilities or contracts which are required for the operation of the Business, other than the Assets, Liabilities and Contracts.

2.8 Neither the Division nor a Change of Control of FRISK will result in the termination of, or have any material effect on, any of the Assets, the Liabilities and/or the Contracts.

3. INFORMATION

3.1 All information contained in the Disclosure Documentation is complete, accurate and not misleading.

3.2 There is no information of material importance that the Sellers are aware of which has not been Disclosed.

3.3 The particulars relating to the Company, FRISK and the Business in this Agreement are true, correct and not misleading.

4. COMPLIANCE WITH LAWS

4.1 The Company and FRISK have at all times conducted their business in all material respects in accordance with all applicable laws and regulations.

5. LICENSES AND CONSENTS

5.1 The Company has all necessary governmental or regulatory or other licenses, consents, permits and authorities necessary to carry on the Business.

5.2 So far as the Sellers are aware, there is no reason why any of those licenses, consents, permits and authorities should be suspended, cancelled, revoked or not renewed on the same terms.

6. INSURANCE

6.1 All the insurance policies maintained in respect of the Business are set out in the Due Diligence Documentation.

6.2 As at Completion, the Company has sufficient cover against all losses and liabilities including business interruption and other risks that are normally insured against by a person carrying on the same type of business as the Company.

6.3 There are no outstanding claims under, or in respect of the validity of, any of those policies and there are no circumstances likely to give risk to any claim under those policies.

6.4 All the insurance policies are in full force and effect, are not void or voidable, nothing has been done or not done which could make any of them void or voidable and neither the Division nor the Transaction will terminate, or entitle any insurer to terminate, any such policy.

7. POWER OF ATTORNEY

7.1 There are no powers of attorney in force given by the Company or by FRISK in respect of the operation of the Business.

7.2 No person, as agent or otherwise, is entitled or authorized to bind or commit the Company or FRISK (in respect of the Business), other than as stipulated in the Company's articles of association.

8. DISPUTES AND INVESTIGATIONS

8.1 Neither the Company nor FRISK is engaged in any litigation, administrative, mediation or arbitration proceedings or other proceedings or hearings before any statutory or government body, department, board or agency (except for debt collection in the normal course of business).

8.2 Neither the Company nor FRISK is subject to any investigation, inquiry or enforcement proceedings by any government, administrative or regulatory body.

8.3 No proceedings, investigation or inquiry as are mentioned in paragraph 8.1 or paragraph 8.2 of this Schedule 5 have been threatened or are pending and there are no circumstances likely to give rise to any such proceedings.

9. THE COMPANY'S AND FRISK'S PRODUCTS

9.1 No proceedings have been started, are pending or have been threatened against either the Company or FRISK in which it is claimed that a product by the applicable company is defective, not appropriate for its intended use or has caused material damage to any person or property when applied or used as intended.

9.2 No proceedings have been started and there are no outstanding liabilities or claims pending or threatened against either the Company or FRISK in respect of any services supplied by the applicable company for which such company is or may become liable and no dispute exists between such company and any of their respective customers or clients.

10. MATERIALLY ADVERSE CHANGES

10.1 In the prior 12 months ending with the date of this Agreement, the Business has not been materially affected in an adverse manner.

11. CONTRACTS

11.1 Neither the Company nor FRISK (in respect of the Business) is party to or subject to any agreement or arrangement, including any Contract, which:

(a) is of an unusual or exceptional nature; or

(b) is not in the ordinary and usual course of business of the Company or FRISK; or

(c) may be terminated as a result of any Change of Control of the Company or FRISK; or

(d) may be terminated as a result of the Division or the Transaction;

(e) so far as the Sellers are aware, restricts the freedom of the Company following Completion to carry on the whole or any part of the Business in any part of the world in such manner as it thinks fit; or

(f) involves agency or distributorship; or

(g) involves partnership, joint venture, consortium, joint development, shareholders or similar arrangements; or

(h) is incapable of complete performance in accordance with its terms within six months after the date on which it was entered into; or

(i) cannot be readily fulfilled or performed by the Company or FRISK on time without undue or unusual expenditure of money and effort; or

(j) requires the Company or FRISK to pay any commission, finders' fee, royalty or the like.

11.2 Each Contract is in full force and effect and binding on the parties to it, and neither the Company nor FRISK have defaulted under or breached a Contract and to the best of each of the Seller's knowledge:

(a) no other party to a Contract has defaulted under or breached such a contract; and

(b) no such default or breach by the Company or FRISK or any other party is likely or has been threatened.

11.3 No notice of termination of a Contract has been received or served on either the Company or FRISK or any other party to a Contract and, to the best of the each of the Seller's knowledge, there are no grounds for termination, rescission, avoidance or repudiation of any such contract.

11.4 The Contracts constitute all of the agreements or arrangements which are of material importance for the Business.

12. TRANSACTIONS WITH THE SELLERS

12.1 The definition in this paragraph applies in this Agreement.

Connected: a person or a party shall be deemed to be connected with any of the Sellers if that person is connected with the any of the Sellers as a person connected with an insider within the meaning of section 16 of Rules no. 987/2006 of the Icelandic Financial Supervisory Authority.

12.2 Other than the loan from the Sellers to FRISK for an amount of around ISK 60-70 million as at the date of this Agreement, and the Lease Agreement, there is no outstanding indebtedness or other liability (actual or contingent) and no outstanding contract, commitment or arrangement between either the Company or FRISK and the Sellers or any person or party Connected with the Sellers.

12.3 No person or party Connected with the Sellers is entitled to a claim of any nature against the Company or FRISK, or has assigned to any person the benefit of a claim against the Company or FRISK to which the Sellers or any person or party Connected with the Sellers would otherwise be entitled.

13. FINANCE AND GUARANTEES

13.1 Neither the Company, nor FRISK, has any liabilities other than the Liabilities and for the avoidance of doubt, no guarantee, mortgage, charge, pledge, lien assignment or other security agreement or arrangement has been given by or entered into by the Company, FRISK, or any third party in respect of other obligations of the Company or FRISK.

13.2 The Sellers are not aware of any reason why any debts owing to the Company or FRISK (in respect of the Business) (including account receivables) have either prior to the date of this Agreement been realized or will not, within three months after the date of this Agreement, realize in cash their full amount and none of those debts or any part of them has been outstanding for more than two months from its due date for payment.

13.3 Neither the Company nor FRISK is responsible for the indebtedness, or for the default in the performance of any obligation, of any other person.

13.4 As at Completion, the Company has sufficient Working Capital consisting of a minimum of ISK 25,000,000 (or the equivalence thereof in other currencies) in cash.

14. INSOLVENCY

14.1 Neither the Company nor FRISK is insolvent or unable to pay its debts within the meaning of the insolvency legislation applicable and has not stopped paying its debts as they fall due.

15. ASSETS

15.1 The Company is the full legal and beneficial owner of and has good marketable title to all of the Assets.

15.2 The Company is at Completion in possession and control of all of the Assets.

15.3 None of the Assets, undertaking or goodwill of the Company is subject to an Encumbrance, or to any agreement or commitment to create an Encumbrance, and no person has claimed to be entitled to create such an Encumbrance.

15.4 The Assets comprise all the assets necessary for the continuation of the Business.

15.5 None of the Assets is the subject of any lease, lease hire agreement, hire purchase agreement or agreement for payment on deferred terms or is the subject of any license or functioning arrangement.

16. INTELLECTUAL PROPERTY

16.1 As at Completion the Company is the sole legal and beneficial owner, and is in full possession and control, of the IP Assets, free from any Encumbrances.

17. INFORMATION TECHNOLOGY

17.1 The definitions in this paragraph apply in this Agreement.

IT Contracts: all arrangements and agreements under which any third party provides any element of, or services relating to, the IT System, including leasing, hire purchase, licensing, maintenance and services agreements.

IT System: all computer hardware (including network and telecommunications equipment) and material third party non-proprietary software (including associated preparatory materials, user manuals and other related documentation) owned, used, leased or licensed by or to FRISK (in respect of the Business) or to the Company.

17.2 As at Completion the Company has all the hardware and software licenses necessary to use the IT System to carry on the Business as conducted at the date of this Agreement.

17.3 Except to the extent provided in the IT Contracts, as at Completion the Company is the owner of and in possession of the IT System free from encumbrances and all other rights exercisable by third parties.

17.4 The IT Contracts are valid and binding and so far as the Sellers are aware, no act or omission has occurred which would, if necessary with the giving of notice or lapse of time, constitute a breach of any such contract.

17.5 Neither FRISK nor the Company has received any notice in respect of any claims, disputes or proceedings arising or threatened under any IT Contracts.

17.6 The IT Contracts are freely transferable and none of them are liable to be terminated or otherwise materially affected by the Division or a Change of Control of the Business, and the Sellers have no reason to believe that any IT Contracts will not be renewed on the same or substantially the same terms when they expire.

17.7 The elements of the IT System:

(a) are functioning properly and operate substantially as intended;

(b) are not defective in any respect; and

(c) have sufficient capacity and performance to meet the current business requirements of the Business;

(d) include sufficient user information to enable reasonably skilled personnel in the field to use and operate the IT System without the need for further assistance; and

(e) have been satisfactorily and regularly maintained and the IT System has the benefit of appropriate maintenance and support agreements.

17.8 FRISK, and following the Division the Company have implemented appropriate procedures, including in relation to off-site working where applicable, for ensuring the security of the IT System and the confidentiality and integrity of all data stored in it.

17.9 FRISK, and following the Division the Company have in place a disaster recovery plan which is fully documented and would enable the Business to continue if there were significant damage to or destruction of some or all of the IT System.

18. DATA PROTECTION

So far as the Sellers are aware, each of FRISK and the Company have fully complied with the requirements of all applicable legislation concerning rights in respect of privacy and personal data.

19. EMPLOYMENT

19.1 Details of the Employees and the contracts of employment for all of the Employees are set out in the Disclosure Letter.

19.2 There is no notice outstanding that terminates the contract of employment of any Employee of the Company and no dispute outstanding between FRISK or the Company and any of its current or former Employees relating to their employment.

19.3 No offer of a contract of employment has been made by FRISK or the Company to any individual which has not yet been accepted or which has been accepted but where the individual's employment has not yet started.

19.4 The acquisition of the Shares by the Buyer or compliance with the terms of this Agreement will not, so far as any Sellers are aware, cause any directors or senior Employees to terminate their employment.

19.5 All contracts of employment with the Employees are terminable on three months' notice or less without compensation (except compensation payable under the applicable law).

19.6 No Employee has been offered or granted any share option, profit sharing, bonus, commission or any other scheme relating to the profit or sales of the Business.

19.7 No liability has been incurred in the 12 months prior to Completion by the Business in connection with any termination of employment of its Employees (including redundancy payments), or for failure to comply with any order for the reinstatement or re-engagement of any Employee. No such liability is outstanding at Completion.

19.8 Except as provided or allowed for in the Accounts, no former director or Employee, or the dependants of any of those people, has been offered or granted a payment by the Business in connection with the actual or proposed termination or suspension of employment or variation of an employment contract.

19.9 Insofar as they apply to its Employees, FRISK and the Company have complied in all material respects with any:

(a) legal obligations;

(b) codes of conduct or practice; and

(c) collective agreements, customs and practice.

19.10 Neither FRISK nor the Company is involved in any material industrial or trade dispute or negotiation regarding a claim with any trade union or other group or organization representing Employees and, so far as any Seller is aware, there is nothing likely to give rise to such a dispute or claim.

20. COMMTOUCH SHARES

Each of the Sellers represents, warrants and covenants that he or she will comply with the warranties set out in the Share Subscription Letter.

21. ACCOUNTS

21.1 The definitions in this paragraph apply in this Agreement.

Accounts: the audited accounts of FRISK for the financial years ending on 31 December 2010 and 31 December 2011 respectively and the annexed directors' and auditors' reports.

Taxation: all forms of taxation including, in particular, any charge, tax, duty, levy, impost, withholding or liability wherever chargeable imposed for support of national, state, federal, municipal or local government or any other person in

any jurisdiction and any penalty, fine, surcharge, interest, charges or costs payable in connection with any such taxation.

21.2 The Accounts have been prepared in accordance with the accounting standards, principles and practices generally accepted in Iceland and in accordance with the law of that jurisdiction.

21.3 The Accounts have been audited by an auditor of good repute qualified in Iceland and the auditor has given an auditor's certificate without qualification.

21.4 The Accounts:

(a) make proper and adequate provision or reserve for all bad and doubtful debts, obsolete or slow-moving inventories and for depreciation on non-current assets;

(b) do not overstate the value of current or non-current assets; and

(c) do not understate any liabilities (whether actual or contingent).

21.5 The Accounts show a true and fair view of the commitments and financial position and affairs of FRISK as at 31 December 2010 and 31 December 2011.

21.6 The Accounts contain either provision adequate to cover, or full particulars in notes of, all Taxation (including deferred taxation) and other liabilities (whether quantified, contingent, disputed or otherwise) of FRISK on 31 December 2010 and 31 December 2011.

21.7 The Accounts are not affected by any unusual or non-recurring items or any other factor that would make the financial position and results shown by the Accounts unusual or misleading in any material respect.

21.8 The Accounts will be filed in accordance with the law of Iceland following approval by the Sellers at the next annual general meeting of FRISK.

21.9 The Accounts have been prepared on a basis consistent with the audited accounts of, as the case may be, FRISK for the two prior accounting periods without any change in accounting policies used.

22. FINANCIAL AND OTHER RECORDS

22.1 All financial and other records relating to the Business and the Company:

(a) have been properly prepared and maintained;

(b) constitute an accurate record of all matters that ought to appear in them;

(c) do not contain any material inaccuracies or discrepancies; and

(d) are in the possession of the Company at Completion.

22.2 No notice has been received or allegation made that any of those records are incorrect or should be rectified.

22.3 All statutory records required to be kept or filed in respect of the Business have been properly kept or filed and comply with all material requirements of any applicable legislation.

22.4 All statutory records and original deeds belonging to the Company shall be in the possession of the Company at Completion.

23. CHANGES SINCE 31 DECEMBER 2011 UNTIL IMMEDIATELY PRIOR TO THE DIVISION

Since 31 December 2011:

(a) FRISK has conducted its business in the normal course and as a going concern;

(b) there has been no material adverse change in the Working Capital, turnover, indebtedness, financial position or prospects of FRISK;

(c) FRISK has not issued or agreed to issue any share or loan capital except as a result of the transaction contemplated by this Agreement and agreed between the Parties;

(d) no dividend or other distribution of profits or assets has been, or agreed to be, declared, made or paid by FRISK;

(e) FRISK has not borrowed or raised any money or taken any form of financial security, and no capital expenditure has been incurred on any individual item by FRISK outside the normal course of business and FRISK has not acquired, invested or disposed of (or agreed to acquire, invest or dispose of) any individual item by FRISK outside the normal course of business; and

(f) no shareholder resolutions of FRISK has been passed other than as routine business at the annual general meeting.

24. EFFECT OF SALE OF SHARES

Neither the acquisition of the Shares by the Buyer nor compliance with the terms of this Agreement will:

(a) give rise to, or cause to become exercisable, any right of pre-emption over the Shares; or

(b) entitle any person to receive from the Company any finder's fee, brokerage or other commission in connection with the purchase of the Shares by the Buyer; or

(c) entitle any person to acquire, or affect the entitlement of any person to acquire, any Shares; or

(d) as far as the Sellers are aware of, result in any customer or supplier being entitled to reduce substantially its existing level of business or to change the terms on which it deals with the Company; or

(e) so far as any Seller is aware, result in any senior employee leaving the Company; or

(f) result in a breach of law, regulation, order, judgment, injunction, undertaking, decree or other like imposition; or

(g) result in the creation, imposition, crystallization or enforcement of any Encumbrance on any Assets or any other assets of the Company.

25. TAXES

25.1 No Tax will be levied on the Company and/or the Buyer Group in relation to the Division or due to FRISK activities prior to the Division.

25.2 No Tax will be levied on the Company and/or the Buyer Group due to the sale of the Shares or the IP Assets.

SCHEDULE 6 Particulars of the Earnout

1. INTERPRETATION

1.1 The definitions in this paragraph 1.1 apply in this Schedule 6.

Earn-out Period: the period from Completion and ending on 31 March 2015.

Excluded Revenues: the revenues for Zero-Hour Virus Outbreak Detection and any revenues that were previously paid as royalties in the contract agreement between FRISK and Commtouch Inc.

Revenues: the combined revenues for sales of antivirus products by the Buyer's Group (including the Company), including for F-Prot and Command, as calculated in accordance with the revenue recognition rules referred to in paragraph 2 below. For the avoidance of doubt, "Revenues" shall not include any Excluded Revenues.

2. REVENUE RECOGNITION RULES

2.1 U.S. GAAP accounting guidance EITF 08-1 is the guidance that the Buyer will use in determining the recognition of the Revenues.

2.2 Where the Company provides services to customers following Completion under certain Contracts for which deferred revenues were previously recognized and payments were received by FRISK or the Company prior to Completion, as specified in the Disclosure Letter, such deferred revenue shall not be included in the calculation of Revenue.

3. PROCEDURE FOR MAKING EARN-OUT PAYMENTS

3.1 Promptly following the completion of the audited financial statements for each of the years ended 31 December 2012, 31 December 2013 and 31 December 2014, and in respect of the first quarter of 2015, the filing of the quarterly results to the SEC, the Buyer shall prepare and deliver to the Sellers a schedule (the "**Earn-out Determination Schedule**") setting forth the Revenues and the figure that represents 5% of the Revenues (the "**Earn-out Payment**") for such calendar year (collectively the "**Earn-out Payments**").

3.2 For the avoidance of doubt, the Earn-out Payment for the year 2012 will be calculated from the Revenues created between Completion and 31 December 2012 while the Earn-out Payments for the years 2013 and 2014 will be calculated on a full calendar year basis, and the Earn-out Payments for 2015 will be calculated only in respect to the first quarter of 2015.

3.3 The Earn-out Determination Schedule shall be conclusive and binding upon the Sellers save in the event of manifest error. Notwithstanding the foregoing, should the Sellers have a reason to believe that the calculation of the Earn-out Payment in the Earn-out Determination Schedule does not correctly represent a figure that is in fact 5% of the Revenues, the Sellers are permitted to have their accountant

enter the Buyer's accountancy to certify that the Revenues that the calculation is based on has been correctly stated. Said right shall be available to Sellers for exercise within 45 days following delivery of each Earn-out Determination Schedule, and shall only enable Sellers to certify the Earn-out Determination Schedule covering the then prior year. Should such examination show that the Buyer under-reported Revenues by greater than 3%, the Buyer shall bear the cost of such examination; otherwise, the Sellers shall bear the cost of such examination.

3.4 Should the examination of the Sellers' accountant lead to a figure greater than the Revenues figure that the Buyer had originally stated and the Buyer is not satisfied with such examination, in the absence of mutual agreement of the issue by the parties, the Buyer and the Sellers shall agree on the appointment of an independent expert and agree on his terms of appointment to resolve the dispute.

3.5 If the Buyer and the Sellers are unable to agree on the appointment of an expert or his terms of appointment within fourteen days of either party serving details of a suggested expert on the other, either party may request the President of the Institute of chartered Accountants of England and Wales to appoint an Expert who is a qualified chartered accountant that has experience in U.S. GAAP accounting and agree on the reasonable terms of appointment with such expert.

3.6 The expert is required to prepare a written decision and give notice (including a copy) of the decision to the parties within a maximum of two months of the matter being referred to the expert.

3.7 The parties are entitled to make written submissions to the expert. The expert's written decision on the matters referred to him shall be final and binding on the parties in the absence of manifest error or fraud.

3.8 Each party shall bear its own costs in relation to the expert. The expert's fees and any costs properly incurred by him in arriving at his determination shall be borne as determined by the expert. Should the expert confirm the Buyer's original calculation (or that the Buyer's calculation is within a 3% margin of error), the Buyer is not obligated to bear the cost of the examination of the Sellers' accountant.

3.9 Subject to clause 6.3, the Buyer shall pay each Earn-out Payment to the Sellers Account (or such other account as may be notified by the Sellers' no less than 10 Business Days prior to such payment) within 10 Business Days following provision of the Earn-out Determination Schedule.

SCHEDULE 7 – Post-Completion Adjustments

1 Adjustment in respect to the cash balance of the Company at Completion.

1.1 In the event that the cash balance of the Company exceeds ISK 25,000,000 at Completion, the surplus shall be transferred to FRISK. FRISK shall be entitled to cash balance that exceeds ISK 25,000,000 and is below ISK 44,000,000. However, any amount exceeding ISK 44,000,000 shall remain with the Company.

1.2 In the event that the cash balance of the Company is less than ISK 25,000,000 (or the equivalence thereof in other currencies) at Completion, the Buyer is entitled to deduct the difference between (i) ISK 25,000,000 and (ii) the cash balance of the Company at Completion, from the Completion Payment (using the mid-rate of the Central Bank at the date of Completion).

1.3 The Sellers undertake to conduct the Business (including the business of the Company) in the ordinary course of business consistent with past practice and with the view to maintain the business as a going concern and not to do anything, either by act or omission, which will have an adverse effect on the cash balance of the Company at Closing.

IN WITNESS whereof this Agreement has been executed on the date first above written.

On behalf of **COMMTOUCH SOFTWARE LTD.**

By: /s/Shlomi Yanai

By:

/s/Friðrik Skúlason

/s/Björg Marta Ólafsdóttir

Exhibit 4.7

Exhibit I

Purchase and Assignment Agreement

relating to shares in

eleven Gesellschaft zur Entwicklung und Vermarktung

von Netzwerktechnologien mbH

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b e t w e e n

1) **Robert Rothe,**
whose address is Berlin

– hereinafter **"Seller 1"** or **"Representative"**–

2) **Benjamin Pannier,**
whose address is Berlin

3) **Robert Strycharczuk,**
whose address is Berlin

4) **Ragna Rothe,**
whose address is Berlin

5) **Jörg Jacobs,**
whose address is Berlin

– the parties referred to under 1) through 5) hereinafter each a **"Seller"** and collectively the **"Sellers"**–

a n d

6) **Commtouch Germany GmbH & Co. KG** (currently still acting under the trade name: cor 29. GmbH & Co. KG), with registered seat in Berlin, registered with the commercial register at the local court of Berlin (Charlottenburg) under docket number HRA 47286 B, represented by its general partner Commtouch Management GmbH (currently still acting under the trade name: aptus 754. GmbH), with registered seat in Berlin, registered with the commercial register at the local court of Berlin (Charlottenburg) under docket number HRB 144201 B, represented on its part by managing director Shlomo Yanay on sole signature

– hereinafter **"Purchaser"**–

7) **Commtouch Software Ltd.,** a company incorporated under the laws of the State of Israel, listed on the NASDAQ Stock Exchange under the symbol CTCH

– hereinafter **“Commtouch”**–

– the Sellers, Commtouch and the Purchaser collectively hereinafter **“Parties”**–

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Table of Definitions

1 Preamble

1.1 eleven Gesellschaft zur Entwicklung und Vermarktung von Netzwerktechnologien mbH is a German limited liability company (*Gesellschaft mit beschränkter Haftung - GmbH*) and incorporated and existing under the laws of Germany, located in Berlin, Germany and registered with the commercial register of the local court of Berlin (Charlottenburg) under HRB 83892 B (hereinafter referred to as "**Company**").

1.2 The Company has a total share capital of EUR 60,000. The share capital consists of five shares with the serial numbers 1 through 5 having a nominal value of EUR 38,600 (serial number 1), EUR 7,300 (serial number 2), EUR 7,300 (serial number 3), EUR 3,500 (serial number 4) and EUR 3,300 (serial number 5) (collectively: the "**Shares**"). The Sellers are all of the shareholders of the Company. holding the Shares as set out in the shareholders' list attached to the Reference Deed as **Annex 1.2**.

1.3 The Company wholly owns two subsidiaries: (i) eleven – internationale Vertriebsgesellschaft mbH, a limited liability company under German law with business seat in Berlin, registered with the commercial register of the local court of Berlin (Charlottenburg) under HRB 100313 B and (ii) eleven USA Inc., a Delaware corporation.

1.4 The Purchaser is an indirectly wholly owned subsidiary of Commtouch.

1.5 The Purchaser intends to purchase the Shares from the Sellers ("**Transaction**").

1.6 The Parties are aware that according to Section 19 (4) of the articles of association of the Company the disposal over shares requires the authorization of the Company's shareholder meeting. The Company's shareholder meeting has approved the Transaction with shareholder resolution dated 12 November 2012 and the Company has on that basis granted its consent to the transfer of all Shares by written declaration dated ___ November 2012. Copies of such shareholder resolution and written declaration are for documentary purposes (zu Beweiszwecken) attached to the Reference Deed as **Annex 1.6**

2 Sale and Assignment

2.1 Each Seller hereby sells (*verkaufen*) his or her respective Share to the Purchaser. The Purchaser accepts the sale of the Shares.

2.2 Each Seller hereby assigns (*treten ab*) his or her respective Share, subject to the conditions precedent (*aufschiebende Bedingungen*) within the meaning of § 158 (1) German Civil Code (*BGB*) of satisfaction or waiver of the Conditions Precedent as described in Section 6. The Purchaser hereby accepts such conditional assignment of the Shares.

2.3 The assignment of the Shares is made with economic effect as of the Closing Date (as defined in Section 6.2 below) and shall include all ancillary rights

appearing thereto, in particular the rights to any undistributed profits from any periods prior to the Closing Date and the right to receive dividends, as of the beginning of the current financial year.

2.4 Each of the Sellers confirms that the Shares held by such Seller do not constitute his or her entire, or nearly (90% or more) his or her entire, property. Furthermore, the Purchaser, having been pointed by the notary to the provisions of Section 1365 of the German Civil Code declared that he has neither been made familiar nor is otherwise familiar with the financial situation of any of the Sellers.

2.5 Commtouch confirms to procure that, as of the Closing Date (as defined in Section 6.2 below) and at least until expiry of the last Measurement Period (as defined in Section 4.4 below), the Company will remain a German entity, irrespective of the particular legal form (e.g. a limited liability company (*Gesellschaft mit beschränkter Haftung – GmbH)*, a company limited by shares (*Aktiengesellschaft – AG*) or a limited partnership (*GmbH & Co. KG*)), that is neither directly nor indirectly controlled by a United States entity. The Parties will use commercially reasonable efforts to safeguard that the Company will not become subject to any foreign (non-German, in particular United States or United Kingdom) data protection laws or to investigation rights of authorities of foreign (non-German, in particular United States or United Kingdom) authorities in a manner that is likely to materially adversely affect the business of the Company.

3 Initial Purchase Price

3.1 The aggregate initial purchase price to be paid by the Purchaser for the Shares amounts to EUR 9,878,172 (in words: Nine Million Eight Hundred Seventy Eight Thousand One Hundred and Seventy Two Euros) (the "**Initial Purchase Price**").

3.2 The Initial Purchase Price shall be comprised of:

3.2.1 cash in the amount of EUR 8,231,810 (in words: Euro Eight Million Two Hundred Thirty One Thousand Eight Hundred and Ten) (the "**Cash Consideration**"); and

3.2.2 such number of restricted ordinary shares, with a nominal par value of NIS 0.15 per share, in Commtouch, having a value as determined in Section 3.2.2.1 below of EUR 1,646,362 (in words: One Million Six Hundred Forty Six Thousand Three Hundred and Sixty Two Euros) (the "**Equity Consideration**"). The Cash Consideration and the Equity Consideration shall be paid to the Sellers on a pro rata basis, in proportion to their shareholdings in the Company as of the Closing Date and in accordance with the terms of this Agreement, unless otherwise expressly stipulated. In the event that the pro rata number of shares to be allocated to one or more Sellers is not an integral number, Seller 1 shall determine whether the number of shares of Equity

Consideration to be allocated to any specific Seller shall be rounded up or rounded down, *provided* that the aggregate number of shares of the Equity Consideration shall not exceed the number determined prior to such rounding.

3.2.2.1 The actual number of the shares of the Equity Consideration shall be based on (i) the average share price of the shares in Commtouch during the twenty (20) trading days (New York) preceding the earlier of (a) the date of this agreement or (b) the date of the public announcement of the Transaction and (ii) the closing EURO-US dollar market exchange rate in effect on the currency trading day prior to Closing Date, as published on Bloomberg. If the number of shares so determined shall be a fractional share, then the number shall be rounded up if the fraction is ½ or greater, and otherwise shall be rounded down.

3.2.2.2 The shares of the Equity Consideration shall vest (i.e. confer unrestricted shareholder rights as set out in the last sentence of this Section 3.2.2.2) in two equal annual installments as follows: (i) the first installment of 50% of the Equity Consideration shall vest immediately upon the 12-month anniversary of the Closing; and (ii) the second installment of the remaining 50% of the Equity Consideration shall vest immediately upon the 24-month anniversary of the Closing. Each vested share of the Equity Consideration shall enjoy standard shareholders' rights, identical to those of the shares in Commtouch, subject to applicable corporate and securities laws and the terms hereof.

3.2.2.3 Restrictions on Transfer. Any transfer of the Equity Consideration must comply with all applicable securities laws, and the Parties agree that the Sellers may be required to provide a satisfactory opinion of counsel to this effect, without incurring any further expenses for the Sellers. The Purchaser may issue appropriate "stop-transfer" instructions to its transfer agent, American Stock Transfer & Trust Company, to prevent the violation of applicable securities laws.

3.2.2.4 The shares of the Equity Consideration shall be issued at the Closing in "book entry" format with the Purchaser's transfer agent. The certificates evidencing the Equity Consideration issued pursuant to this Agreement will bear the following legend reflecting the foregoing restrictions on the transfer of such securities, in addition to any legend required by applicable U.S. state securities laws:

"**THESE SECURITIES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED. THEY MAY NOT BE SOLD, OFFERED FOR SALE, TRANSFERRED, PLEDGED OR HYPOTHECATED IN THE ABSENCE OF A REGISTRATION STATEMENT IN EFFECT WITH RESPECT TO THE SECURITIES UNDER SUCH ACT OR AN OPINION OF COUNSEL OR OTHER EVIDENCE SATISFACTORY TO THE COMPANY THAT SUCH REGISTRATION IS NOT REQUIRED OR UNLESS SOLD PURSUANT TO RULE 144 UNDER SUCH ACT.**"

3.2.2.5 Removal of Legend. The Equity Consideration will no longer be subject to the legends referred to in Section 3.2.2.4 above upon the termination or lapse of all restrictions and conditions on transfer under applicable securities laws or pursuant to a disposition that is permitted thereunder. After such time, and upon the Seller's request, a new certificate or certificates representing such Seller's pro rata portion of the Equity Consideration held in such Seller's name shall be issued without the legends referred to above and delivered to such Seller, provided that Commtouch is provided with all certificates, opinions and other information it may reasonably request in connection with such request.

3.3 The Sellers represent and warrant that prior to the date of this Agreement they have (i) repaid all loans that they took from the Company without any remaining mutual claims arising therefrom and (ii) reimbursed the Company for any expenses that should be borne by the Sellers pursuant to Section 12 below and which have been incurred by the Company.

3.4 At the Closing (as defined in Section 6.2 below), the Purchaser shall transfer to each of the Sellers its pro rata portion of the Closing Cash Payment (as defined below) to the respective bank account as set forth opposite each Seller's name in **Annex 3.4a)** to the Reference Deed. The "**Closing Cash Payment**" shall mean an amount of EUR_____ (in words:_____) which equals the Cash Consideration (i) minus EUR 823,181 (in words: Eight Hundred Twenty Three Thousand One Hundred and Eighty One Euros) (the "**Escrow Amount**") and (ii) minus or plus, as the case may be, any Cash and Deferred Revenue Adjustment (as defined in Section 3.6 below). The definite the calculation of the Closing Cash Payment and the Cash and Deferred Revenue Adjustment, including the Closing Cash Certificate (as defined in Section 3.6.3 below), is shown in **Annex 3.4b)**.

3.5 "**Business Day**" shall mean each day that is not a Friday, Saturday or Sunday, or on which banking institutions located in Tel Aviv, Israel, Berlin, Germany, or in the State of California are authorized or obligated by law to close. The Sellers represent and warrant that there are no expenses that should be

borne by the Sellers pursuant to Section 12 below, which either were paid by the Company on or prior to the date of this Agreement or that are to be paid by the Company after the date of this Agreement.

3.6 Cash and Deferred Revenue Adjustment.

3.6.1 The Company is obligated to provide services to customers for whom deferred revenues were recognized and respective pre-payments were received by the Company prior to Closing. The Sellers shall ensure that the Company's cash and cash equivalents (*i.e.* free cash in bank accounts, and corporate commercial paper and other money market instruments that can easily be converted into cash, including sums invested in money and financial markets (*Geldmarkt*), collectively referred to as "**Cash**"), excluding any cash needed to settle the payment obligations of the Company to former holders of Company Options as described in Section 3.9, at Closing shall at least equal the pre-payments for deferred revenues at Closing.

3.6.2 The Sellers hereby guarantee to Purchaser that since December 31, 2011, and continuing through the Closing, the overall average amount of liabilities and receivables of the Company has changed and will change only in the ordinary course of business and consistent with past practice, and the Company has not borrowed any funds.

3.6.3 The Cash and Deferred Revenue Adjustment included in Annex 3.4b) reflects the Company's good faith best estimate (based on reasonable assumptions) of (i) the amount of pre-payments for deferred revenues at Closing, and (ii) the amount of Cash in the Company at Closing, (the "**Company Closing Cash Certificate**"). For the avoidance of doubt, the Company Closing Cash Certificate has been prepared in view of all payment obligations to former holders of Company Options as described in Section 3.9 having to be paid as of Closing by the Company from the cash available in the Company at that time. The Company Closing Cash Certificate shall fairly and accurately present the Company's good faith best estimate (based on reasonable assumptions). The Company Closing Cash Certificate shall be used by the Purchaser (i) to reduce the Closing Cash Payment payable pursuant to this Agreement to the extent, if any, that the Cash shall be less than the pre-payments for deferred revenues at Closing, or (ii) to increase the Closing Cash Payment payable pursuant to this Agreement to the extent, if any, that the Cash shall exceed the pre-payments for deferred revenues at Closing.

3.6.4 The correctness of the Company Closing Cash Certificate shall be treated as a representation and warranty by the Sellers for all purposes, and any inaccuracy in such Company Closing Cash Certificate shall give rise to all of the remedies available for a

misrepresentation. Section 8 shall apply *mutatis mutandis* with the exception that deviating from Section 8.1 the representation and warranty of the correctness of the Company Closing Cash Certificate shall expire one month after the publication of the Purchaser's audited financial statements for the year ending December 31, 2012, but not later than May 31, 2013.

3.7 At the Closing (as defined in Section 6.2 below) Sellers, Purchaser and Attorney at Law Dr. Johannes Meinel (the "**Escrow Agent**") shall enter into an escrow agreement substantially in the form attached to the Reference Deed as **Annex 3.7.** (the "**Escrow Agreement**") and the Purchaser shall deposit the Escrow Amount with the Escrow Agent in accordance with the terms hereof and the Escrow Agreement in a respective account of the Escrow Agent (the "**Escrow Account**").

3.8 In case the Purchaser has delivered a Claim Certificate pursuant to Section 8.7.1 and the Representative has delivered an Objection Notice pursuant to Section 8.7.2 before the Purchaser's payment of the 2012 Earn-out Payment (as defined in Section 4.4 below), if any, pursuant to Section 4 hereof, an additional amount of EUR 180,000 (in words: One Hundred and Eighty Thousand Euros) shall be deducted from the 2012 Earn-out Payment, if any, and added to the Escrow Amount (the "**Additional Escrow Amount**"). The Escrow Amount and the Additional Escrow Amount, if and to the extent such is deposited by the Purchaser with the Escrow Agent, shall be hereinafter collectively referred to as the "**Escrow Fund**".

3.9 **Treatment of the Profit Participation Option Program (Genussrechtsoptions-programm) (the "Plan")**.

No option or other right granted under the Plan (whether vested or unvested) that is outstanding immediately prior to the Closing (each, a "**Company Option**") shall be assumed by Purchaser. The Sellers have provided to the Purchaser with all of the existing waiver and release agreements *(Vereinbarungen über die Abfindung von Genussrechtsoptionen)*, signed by all of the holders of Company Options, whereby each such holder validly agrees to the termination of the Company Options held by him, subject only to, and effective upon, the Closing, against consideration by the Company ("**Plan Considerations**"); copies of those waiver and release agreements *(Vereinbarungen über die Abfindung von Genussrechtsoptionen)* are for documentary purposes (*zu Beweiszwecken*) attached to the Reference Deed as **Annex 3.9.(b)(1)**. The Parties acknowledge that Commtouch and the Sellers have reached an agreement that the Plan Considerations consist of a cash payment in the aggregate amount of up to **EUR 733,800** to be paid by the Company to the former holders of the Company Options and the provision of option rights in shares in Commtouch according to the current employee option scheme applicable to employees of Commtouch as amended from time to time. Commtouch hereby undertakes to grant the required options to the respective former holders of the Company Options. The Parties are aware of the fact that as a consequence of the cash payment to the former

holders of Company Options the Company will not generate any profit in the fiscal year 2012.

3.10 Any payment under this Agreement shall be deemed to have been effectuated on that date it has been credited to the account of the respective recipient. All payments shall be made free and clear of any costs and bank charges.

4 Earn-out

4.1 Payment of Earn-out Payments. Subject to the terms and conditions of this Agreement, including this Section 4, in addition to the Initial Purchase Price, the Purchaser shall pay or cause to be paid to each of the Sellers its pro rata portion of an amount in cash equal to each of the Annual Earn-out Amounts, if any, determined as specified below and payable without undue delay after the calculation pursuant to Section 4.3 has been completed with respect to the respective Annual Earn-out Amount.

4.2 Annual Earn-out Amounts. Subject to adjustment as provided below, the Annual Earn-out Amount, if any, for any Measurement Period shall be calculated as follows:

2012 Earn-out

4.2.1 On the basis of the 2012 Platform Revenue for the twelve months ending 31 December 2012, the 2012 Earn-out Payment shall be the difference between (A) twice the 2012 Platform Revenue, and (B) the Initial Purchase Price.

2013 – 2015 Earn-out

4.2.2 In the event the sum of the 2013-2015 Platform Revenue and AV Platform Revenue for any Measurement Period is less than EUR 3,122,000, then the Annual Earn-out Amount for such Measurement Period shall be equal to zero.

4.2.3 In the event the sum of the 2013-2015 Platform Revenue and AV Platform Revenue for any Measurement Period is at least EUR 3,122,000 but not more than EUR 5,307,000, then the Annual Earn-out Amount for such Measurement Period shall be equal to

i) 12% of the 2013-2015 Platform Revenue for such Measurement Period squared, divided by EUR 6,244,000, plus

ii) 3% of the AV Platform Revenue for such Measurement Period.

4.2.4 In the event the sum of the 2013-2015 Platform Revenue and AV Platform Revenue for any Measurement Period is more than EUR 5,307,000 but not more than EUR 6,244,000, then the Annual Earn-out Amount for such Measurement Period shall be equal to

i) 12% of the 2013-2015 Platform Revenue for such Measurement Period, plus

ii) 3% of the AV Platform Revenue for such Measurement Period.

4.2.5 In the event the sum of the 2013-2015 Platform Revenue and AV Platform Revenue for any Measurement Period is more than EUR 6,244,000, then the Annual Earn-out Amount for such Measurement Period shall be equal to the sum of:

i) EUR 749,280 (referred to as "**Base Earn-out Amount**"), plus

ii) 10% of the difference between the 2013-2015 Platform Revenue for such Measurement Period and EUR 6,244,000, plus

iii) 3% of the AV Platform Revenue for such Measurement Period ((ii) and (iii) collectively "**Upside Earn-out Amount**").

4.3 Calculation of Annual Earn-out Amounts; Dispute Resolution. As soon as reasonably practicable, but not later than one month following the completion of the audited financial statements for each Measurement Period, the Purchaser shall prepare and deliver to the Representative a statement showing the AV Platform Revenue and the 2013-2015 Platform Revenue or, as the case may be, the 2012 Platform Revenue and the calculation of the Annual Earn-out Amount for such Measurement Period. The Purchaser shall afford to the Representative and its advisors reasonable access during normal business hours and upon reasonable notice after delivery of each Annual Earn-out Calculation Statement to the books of account and records used or that should have been used to prepare the Annual Earn-out Calculation Statement, and to management of the Purchaser, for purposes of verifying the calculation of the Annual Earn-out Amount. The Representative shall notify the Purchaser in writing within twenty (20) Business Days of receipt of an Annual Earn-out Calculation Statement as to whether the Representative disputes the determination of the Annual Earn-out Amount; if the Representative disputes the determination of the Annual Earn-out Amount, the Representative shall deliver an Earn-out Dispute Notice setting forth in reasonable detail the specific items in dispute and the basis for the dispute. If the Representative does not deliver an Earn-out Dispute Notice within twenty (20) Business Days of receipt of an Annual Earn-out Calculation Statement, or if the Representative accepts the amounts set forth in the Annual Earn-out Calculation Statement for the Measurement Period in writing, the Annual Earn-out Amount calculations as contained in the Annual Earn-out Calculation Statement shall be deemed final and binding. In the event an Earn-out Dispute Notice is delivered, the Purchaser and the Representative shall meet within ten (10) Business Days of the delivery of such Earn-out Dispute Notice to attempt to resolve such dispute in good faith. If a final resolution of such dispute is reached as reflected in an agreement in writing, the agreed upon Annual Earn-out Amount agreed with respect to such Measurement Period shall be deemed final and binding. If no final

resolution is reached within fifteen (15) Business Days of the delivery of such Earn-out Dispute Notice after good faith negotiation, either party may require that the dispute (other than a dispute as to the calculation of any aspect of the Annual Earn-out Calculation Statement) be resolved in accordance with the dispute resolution mechanism set forth in Section 13. If the dispute relates to the method of calculation of any aspect of the Annual Earn-out Calculation Statement, the dispute shall be submitted to the Earn-out Arbitrator. The Earn-out Arbitrator shall be authorized only to arbitrate the calculation of the 2012 Platform Revenue, the 2013-2015 Platform revenue and the AV Platform Revenue but shall not have any authority to arbitrate any other dispute relating to the matters addressed in this Section 4.3. The Earn-out Arbitrator shall be instructed to review the Annual Earn-out Calculation Statement, the Earn-out Dispute Notice and all work papers related thereto to determine the Annual Earn-out Amount, and shall use every reasonable effort to determine such amounts within sixty (60) days after the submission of such dispute to it, and in any event as soon as practicable. The Earn-out Arbitrator shall not undertake any review of any matters not specifically identified by the Representative as being in dispute in the Earn-out Dispute Notice and shall only decide the specific items under dispute by the parties and solely in accordance with the terms of this Agreement. In resolving any disputed item, the Earn-out Arbitrator may not assign a value to any item greater than the greatest value for such item claimed by either party or less than the smallest value for such item claimed by either party. The Earn-out Arbitrator's determination shall be based solely on presentations by the Purchaser and the Representative, and an independent review by the Earn-out Arbitrator of the books and records of the Purchaser and on the definitions and other terms included herein. The Earn-out Arbitrator shall set out the resolution of the dispute in writing, which shall be conclusive and binding upon the parties. The costs and expenses of the Earn-out Arbitrator shall be borne (i) by the Purchaser, if the Annual Earn-out Amount as determined by the Earn-out Arbitrator is higher than the Annual Earn-out Amount determined by the Purchaser, (ii) by the Sellers (to be allocated among them on a pro rata basis) if the Annual Earn-out Amount as determined by the Earn-out Arbitrator is lower than the Annual Earn-out Amount as determined by the Representative, or (iii) 50% by the Purchaser and 50% by the Sellers (to be allocated among them on a pro rata basis), in any other case.

4.4 Earn-out Definitions. The following capitalized terms shall have the meanings set forth below:

"**2012 Earn-out Payment**" means the amount, if any, payable pursuant to Section 4.2.1 above.

"**2012 Platform Revenue**" means all revenues (*Umsätze*) of the Company on a consolidated basis (excluding VAT, discounts and credits), determined in accordance with generally accepted accounting principles under German GAAP (HGB) for the twelve months ending 31 December 2012.

"**Annual Earn-out Amount**" means the amount, if any, calculated pursuant to Section 4.2 with respect to each of the Measurement Periods.

"**Annual Earn-out Calculation Statement**" means the statement prepared by Commtouch pursuant to Section 4.3 with respect to each of the Measurement Periods.

"**AV Platform Revenue**" means all revenues (*Umsätze*) of Commtouch on a consolidated basis (excluding VAT, discounts and credits), determined in accordance with generally accepted accounting principles in the United States, in the respective Measurement Period (other than 2012) for any SaaS Technology or Platform relating to

(i) anti virus products and services or

(ii) New SaaS products and services either licensed, acquired or self developed

in each case except for products and services which any Group Company has acquired or licensed as a SaaS Technology or Platform after the conclusion of this Transaction and which is provided to customers in the form acquired without any substantial modifications (other than porting and the like).

"**2013-2015 Platform Revenue**" means all revenues (*Umsätze*) of Commtouch on a consolidated basis (excluding VAT, discounts and credits), determined in accordance with generally accepted accounting principles in the United States, in the respective Measurement Period (other than 2012) for any of the following:

(i) any service or product worldwide, without any qualifications, relating to or deriving from the use of eXpurgate, ensurance, eXached, exelerate, EVA (BSI service) and archiving services, including any future development of such products or services;

(ii) with respect to services or products which derive from the SDK (excluding any SaaS Technology or Platform) currently licensed or sold by the Company, including any future development deriving from any of such SDK ("**Eleven SDK**")

  (a) all amounts invoiced by a Group Company to Eleven SDK Customers worldwide

  (b) all amounts invoiced by a Group Company to any customer in Germany, Austria or Switzerland

(iii) all amounts invoiced by a Group Company to Eleven SDK Customers worldwide with respect to services or products which derive from any SDK (excluding any SaaS Technology or Platform) which is not the Eleven SDK, with the following qualification:

if the relevant Eleven SDK Customer has for a consecutive period of at least twelve months made any revenue with Eleven SDK prior to changing to a different SDK offered by any Group Company, such former revenue made with Eleven SDK (invoiced amounts excluding VAT) shall be deemed to be the revenue made in the relevant Measurement Period rather than the actual revenue made with the new SDK product or service; and

(iv) any e-mail or web service or product worldwide, without any qualifications, relating to or deriving from a SaaS Technology or Platform.

"**Earn-out Arbitrator**" means Deloitte, PricewaterhouseCoopers or another independent accounting firm with offices in Israel and Berlin of recognized international standing, mutually agreed upon by Commtouch and the Representative to resolve disputes relates to the method of calculation of any aspect of the Annual Earn-out Calculation Statement.

"**Earn-out Dispute Notice**" means a notice delivered by the Representative pursuant to Section 4.3, if the Representative disputes the determination of an Annual Earn-out Amount.

"**Eleven SDK Customer**" means all customers of the Company as listed in **Annex 4.4(a)** to the Reference Deed pertaining to the Company's business as referred to in **Annex 4.4(b)** to the Reference Deed.

"**Group Company**" means the Company, Commtouch, or any of Commtouch's direct or indirect subsidiaries worldwide

"**Measurement Period**" means each of (i) the year ending on December 31, 2012, (ii) the year ending December 31, 2013; (iii) the year ending December 31, 2014; and (iv) the year ending December 31, 2015.

"**New SaaS**" means any SaaS Technology or Platform not currently marketed or developed by any Group Company.

"**SaaS Technology or Platform**" means software as a service which is a software delivery model in which software and associated data are centrally hosted on the cloud, cloud computing being the use of computing resources (hardware and software) that are delivered as a service in parts or entirely over the internet.

"**SDK**" means a software development kit which is a set of software development tools that allows for the creation of applications for a certain software package, software framework, hardware platform, computer system, operating system, or similar platform.

4.5 Continuation Requirement.

4.5.1 The Parties agree that Seller 1 shall, as from the Closing Date, remain Employed by the Company. He is intended to remain the Company's managing director (*Geschäftsführer*). Further, he is intended to serve as Commtouch's German site manager and general manager. On the level of Commtouch, Seller 1 shall become Chief Technical Officer ("**CTO**") reporting directly to Commtouch's Chief Executive Officer ("**CEO**"). The consultancy agreement to be entered into, by way of notarial deed (*in notariell beurkundeter Form*), between Purchaser and RoRo Beteiligungsgesellschaft mbH (registered with the commercial register at the local court of Berlin (Charlottenburg) under HRB 117585) at the Closing is attached as **Annex 4.5.1** to the Reference Deed.

4.5.2 Notwithstanding any other provision of this Agreement, if Seller 1 voluntarily resigns from his Employment by the Company on or after January 1, 2013 but within 24 months as from the Closing Date, or is dismissed for "Cause" (as defined in Section 4.5.4 below) at any time, then he shall not be entitled to receive his pro rata share of any Upside Earn-out Amount (if any) calculated pursuant to Section 4.2.5 above with respect to any Measurement Period subsequent to such Measurement Period in which the resignation or dismissal occurs. With respect to the Measurement Period in which such resignation or dismissal occurs, Seller 1 shall (only) be entitled to such proportion of his pro rata share of the respective Upside Earn-out Amount (if any) which equals, pro rata (i) the number of months from the beginning of the Measurement Period up and including the month in which the resignation or dismissal occurs (ii) to 12 months (e.g. in the event the resignation is validly announced in March of the respective Measurement Period, Seller 1 shall only be entitled to 3/12 of the respective Upside Earn-out Amount). For the avoidance of doubt, any Upside Earn-out Amount for past and current Measurement Periods as well as any other portion of a future Base Earn-out Amount which is not an Upside Earn-out Amount shall be unaffected. Any remaining Upside Earn-out Amount of the Measurement Period in which the resignation or dismissal occurs as well as any future Upside Earn-out Amount Seller 1 would be entitled to if he had not resigned shall be deemed to be forfeited to the Purchaser and shall be retained by the Purchaser, and no other Seller shall be entitled to participate in such amount.

4.5.3 Section 4.5.2 shall not apply if Seller 1's Employment by the Company is terminated in any other way (including due to death and/or incapacity for work) as set forth in Section 4.5.2 above, in particular in the event Seller 1 resigns from his Employment by the Company "for cause" – *aus wichtigem Grund* (as defined in Section 626 para. (1) German Civil

Code (*BGB*)) or is dismissed due to an Acceleration Event (as defined in Section 5 below) following the Transaction.

4.5.4 For purposes of Section 4.5.2 above, "Cause" means (for purposes of this definition of Cause, "Commtouch" shall mean any Group Company):

i) an intentional act of fraud, embezzlement, theft or any other material violation of law;

ii) intentional damage to Commtouch's assets;

iii) intentional disclosure of Commtouch's confidential information contrary to company policy;

iv) intentional engagement in any competitive activity which would constitute a breach of a duty of loyalty or of other obligations under an employment agreement;

v) intentional and material breach of any of Commtouch's policies, in effect and as amended from time to time, provided however that such breach would constitute circumstances which under German civil law or employment law would justify a termination "for cause" – *aus wichtigem Grund* (as defined in Section 626 para. (1) German Civil Code (BGB);

vi) the wilful and continued failure to substantially perform duties for Commtouch or the Company, including, but not limited to, repeated unexcused absences from work (other than as a result of incapacity due to physical or mental illness); or

vii) wilful conduct that is demonstrably and materially injurious to Commtouch, monetarily or otherwise.

For purposes of this paragraph, an act, or a failure to act, shall not be deemed wilful or intentional, as those terms are defined herein, unless it is done, or omitted to be done, in bad faith or without a reasonable belief that the action or omission was in the best interest of Commtouch or the Company. Failure to meet performance standards or objectives, by itself, does not constitute "Cause". "Cause" also includes any of the above grounds for dismissal regardless of whether Commtouch learns of it before or after terminating employment or the consultancy agreement (as the case may be).

4.5.5 Nothing contained in this Section 4.5 shall be deemed to detract from the right of Seller 1 to participate in any other Annual Earn-out Amount (in particular the Base Earn-out Amount), including his pro

rata share of any Annual Earn-out Amount calculated pursuant to Sections 4.3 and 4.2.1 to 4.2.5 above. This Section 4.5 contains regulations with regard to the Upside Earn-out Amount only. For the avoidance of doubt, nothing contained in this Section 4.5 shall affect the payment obligations of Purchaser vis-à-vis the other Sellers (not being Seller 1).

4.5.6 For purposes of this Section 4.5, Seller 1 will be deemed to be "**Employed by the Company**" or have an "**Employment by the Company**" so long as he is providing services to any Group Company, either directly or through RoRo Beteiligungsgesellschaft mbH or any other company wholly-owned by Seller 1, pursuant to a consultancy agreement with any Group Company, provided that such arrangement is and continues to be reasonably acceptable to Commtouch.

5 Change of Control Payment

In case any of the events described in Sections 5.1 to 5.4 below occurs within any of the Measurement Periods (each such event referred to as "**Acceleration Event**") Purchaser shall pay on the date of the occurrence of such Acceleration Event to each of the Sellers its pro rata portion of an amount in cash equal to (i) the 2012 Platform Revenue less (ii) all previously paid Upside Earn-out Amounts: and any Upside Earn-out Amount still payable (*fällig und weiterhin zahlbar*) at that time.

5.1 sale, exchange or takeover in an economically comparable way, within 12 months following the Closing, of at least 50% of all Shares in one single transaction and/or multiple transactions in close time proximity by one purchaser and/or consortium of purchasers (with the exception of a respective sale or transfer to a shareholder or a company affiliated to a shareholder within the meaning of sec. 15 et seq. German Stock Corporation Act, *Aktiengesetz – AktG*, or a pure internal group restructuring of the Company and its affiliates provided that at least 50% of the shareholders prior to the restructuring will remain shareholders in any target structure);

5.2 sale, exchange or takeover in an economically comparable way of at least 50% of all of the share capital of Commtouch Software Ltd., in one single transaction and/or multiple transactions in close time proximity by one purchaser and/or consortium of purchasers (with the exception of a respective sale or transfer to a shareholder or a company affiliated to a shareholder within the meaning of sec. 15 et seq. German Stock Corporation Act, *Aktiengesetz – AktG*, or a pure internal group restructuring of the Company and its affiliates provided that at least 50% of the shareholders prior to the restructuring will remain shareholders in any target structure), at a price representing a company value for Commtouch Software Ltd. at least equal to the market value of Commtouch Software Ltd. on the date of the Closing (determined using the guidelines specified in Section 3.2.2.1 above), followed by the announcement of the

termination or end-of-life (or the effective end of active sales activity) of significant SaaS Technology or Platform offerings;

5.3 sale of all or substantially all (at least 75% with respect to fair market value) of the assets of the Company) within 12 months following the Closing; or

5.4 the Company ceases to be a German entity and/or becomes either directly or indirectly controlled by a United States entity.

6 Conditions Precedent

6.1 The assignment of the Shares is subject to the cumulative fulfillment (i) of all Conditions to Closing set forth below and (ii) of all Conditions for Transfer set forth below (the Conditions to Closing and the Conditions for Transfer collectively referred to as the "**Conditions Precedent**"):

6.1.1 Conditions to Closing

i) The Escrow Agreement shall have been signed by the parties thereto.

6.1.2 Conditions for Transfer

i) The Purchaser has paid the Closing Cash Payment according to Section 3.4, as adjusted (if applicable) pursuant to Section 3.6.3;

ii) The Escrow Amount has been paid to the Escrow Account as referred to in Section 3.6; and

iii) The Equity Consideration has been issued by "book entry" according to Section 3.2.2.4.

6.2 The consummation *in rem* of the transactions contemplated in this Agreement ("**Closing**") shall occur when all Conditions Precedent have been fulfilled or have been waived in accordance with Section 6.3. Closing shall occur on 15 November 2012, or on any other day the Parties mutually agree (the "**Closing Date**").

6.3 The Purchaser shall have the right to waive the Condition to Closing referred to in Section 6.1.1 (ii). The waiver is to be declared by the Purchaser in writing to the Representative.

The Sellers, acting through the Representative, shall have the right to waive the Conditions for Transfer in Section 6.1.2 (iii). The waiver is to be declared by the Representative in writing to the Purchaser.

6.4 The Purchaser and the Sellers are entitled to rescind this Agreement by written notice to the respective other Party if the Closing has not occurred by December 31, 2012 at the latest.

6.5 The Parties undertake to use all reasonable endeavors to ensure that the Conditions Precedent are fulfilled as soon as practically possible and when due.

6.6 The Sellers shall deliver to the Purchaser documents evidencing the satisfaction of the Conditions to Closing set out in Section 6.1.1. If all such Conditions Precedent are satisfied, the Purchaser shall send to Mr. Robert Rothe, as the Representative of the Sellers for purposes of this Agreement (the "**Representative**"), a written statement of satisfaction or waiver of the Conditions to Closing set out in Section 6.1.1. Such written statement shall contain a signed copy of the Company Closing Cash Certificate. It also shall contain the intended Closing Date.

6.7 In anticipation of a timely Closing, Purchaser has provided Sellers with the following:

6.7.1 Purchaser delivered to Sellers a scan of a written confirmation by the American Stock Transfer & Trust Company, LLC signed by its Vice President and addressed to Seller 1 confirming that it will issue restricted ordinary shares in Commtouch upon receipt of a corresponding instruction by Commtouch. A copy of the written confirmation is attached to the Reference Deed as **Annex 6.7.1**.

6.7.2 Purchaser delivered to Sellers a written confirmation by Commtouch's General Counsel and Corporate Secretary addressed to Seller 1 confirming that he will on behalf of Commtouch instruct the American Stock Transfer & Trust Company, LLC to issue restricted ordinary shares in Commtouch to Sellers in an amount to be calculated as set forth in Section 3.2.2.1. A copy of the written confirmation is attached to the Reference Deed as **Annex 6.7.2**.

6.8 In order to effectuate the Closing, the Parties shall meet on the Closing Date in the offices of notary public Dr. Peter Wessels, Friedrichstraße 88/Unter den Linden, 10117 Berlin or such other place as agreed by the Parties, and undertake to perform the following actions:

6.8.1 Sellers shall deliver to Purchaser appropriate written proof of the satisfaction of the Conditions to Closing set out in Section 6.1.1;

6.8.2 In case Closing Date should not take place on the same date as the date of this agreement, Sellers shall deliver to Purchaser a revised version of Annex 3.4b amended as of the Closing Date;

6.8.3 Purchaser shall deliver to Sellers appropriate written proof that Purchaser has instructed its bank to immediately wire the Initial Purchase Price into the Sellers' accounts as listed in Annex 3.4 (a) by express wire transfer (*Blitzüberweisung*) and Sellers shall deliver to Purchaser appropriate written proof that the respective amounts of the Initial Purchase Price have been credited to the Sellers' accounts;

6.8.4 Purchaser shall deliver to Sellers appropriate written proof that Purchaser has instructed its bank to immediately wire the Escrow Amount into the escrow account as specified in the Escrow Agreement by express wire transfer (*Blitzüberweisung*) and the Escrow Agent shall

deliver to Purchaser appropriate written proof that the Escrow Amount has been credited to the Escrow Account;

6.9 The Parties shall confirm the fulfilment of the Conditions Precedent by executing a closing memorandum (the "**Closing Memorandum**") at the Closing Date. The attachment of a certified copy (*beglaubigte Abschrift*) of the Closing Memorandum to the original of this Agreement by the acting notary shall constitute the unrebuttable assumption (*unwiderlegbare Vermutung*) that the Closing Conditions have been fulfilled.

6.10 The Parties instruct the acting notary to submit an up-to-date list of the shareholders (*Gesellschafterliste*) of the Company to the relevant commercial register as soon as he has been provided with an original of the signed Closing Memorandum.

7 Representations and Warranties

7.1 Each Seller hereby represents and warrants to the Purchaser by way of an independent guarantee (*selbständiges Garantieversprechen*) within the meaning of § 311 I BGB that the statements set forth below are true and complete at the date of this Agreement and at the Closing Date, unless otherwise specified. The Sellers make the representations and warranties below jointly and severally, except that (i) any representation and warranty made by a Seller as to himself or as to his Shares shall be several and not joint, and (ii) a Seller shall not bear liability greater than the gross amount received by him under this Agreement with respect to his Shares (it being understood that amounts not yet received but receivable in the future may further be offset by the Purchaser against warranty claims provided they do not lead to a payment obligation of the respective Seller beyond the gross amount received by him), except that there shall be no limitation on the liability of any Seller who commits fraud.

7.2 **Status of the Company**. The Company holds the subsidiaries which are referred to in Section 1.3 (Preamble) (each a "**Subsidiary"** and collectively, the "**Subsidiaries**"). The Company and eleven – internationale Vertriebsgesellschaft mbH are limited liability companies under German law (GmbH). eleven USA Inc. is a Delaware corporation. Each of the foregoing companies is duly founded and validly existing, is in good standing under the laws of its foundation (*Gründung*) and has full power to conduct its business as conducted prior to the Closing. The Company has the requisite power and authority to enter into and fully perform its obligations under any agreements entered into pursuant to this Agreement in accordance with their terms. The share capital of the Subsidiaries has been fully paid in.

7.3 **Status of Sellers and Shares**. The Sellers hold unrestricted legal and beneficial title (*uneingeschränkte rechtliche und wirtschaftliche Inhaberschaft*) to the Shares. The Company holds unrestricted legal and beneficial title (*uneingeschränkte rechtliche und wirtschaftliche Inhaberschaft*) to the shares of the Subsidiaries. The Shares and the shares of the Subsidiaries are not pledged

(*verpfändet*), attached (*gepfändet*) or otherwise encumbered (*belastet*) with any Lien (as defined below) or other third party rights. The Shares and the shares of the Subsidiaries are fully paid up. All contributions have been made in compliance with applicable law and have not been partially or totally repaid or returned. There are no obligations to make further contributions in relation to the Shares (*keine Nachschusspflichten*) or the shares of the Subsidiaries. The Shares constitute the entire issued share capital of the Company. No third party has any pre-emptive right (Vorkaufsrecht), right of first refusal (Vorerwerbsrecht), subscription right (Bezugsrecht), option right (Optionsrecht), conversion right (Wandlungsrecht) or similar right in respect of the Shares, and no person has any present, future or contingent right to be entered into the shareholders' register or in the commercial register as the holder of the Shares, any other securities of the Company or the shares of the Subsidiaries and there are no encumbrances on the Shares or the shares of the Subsidiaries or any arrangements or obligations to create any such encumbrances or to issue new shares in the Company or the Subsidiaries. No claim has been made by any person that they are entitled to any such right or have the benefit of any such encumbrances. For purposes of this Agreement, "**Lien**" shall mean any lien, pledge, charge, claim, mortgage, security interest, or other encumbrance of any sort, other than those imposed or applied by applicable Laws. The Purchaser shall not have any liability to any holder of a Company Option under the Plan.

7.4 Business Operations, Business Assets and Loans.

7.4.1 The business of the Company and each Subsidiary is conducted in accordance with all material applicable laws.

7.4.2 Since the respective dates of incorporation, the Company's business operations have been conducted within the ordinary course of business, in accordance with prudent business practice and carried on substantially in the same manner as prior thereto. Since December 31, 2011 the business operations of the Company have not materially adversely changed.

7.4.3 No dividends have been declared, resolved on or distributed by the Company or the Subsidiaries during the current fiscal year.

7.4.4 Neither the Company nor any Subsidiary is responsible for the indebtedness of any other person, nor party to any option or pre-emption right or any guarantee, surety or any other obligation (whatever called) to pay, purchase or provide funds (whether by the advance of money, the purchase of or subscription for shares or other securities or the purchase of assets or services or otherwise) for the payment of, or as an indemnity against the consequence of default in the payment of, any indebtedness of any other person.

7.5 Material Agreements

7.5.1 **Annex 7.5.1** to the Reference Deed contains a true and correct list, as of the date hereof, of all of the following contracts and agreements to

which the Company and each Subsidiary is a party and which have not yet been completely fulfilled (hereinafter referred to as "**Material Agreements**"):

i) agreements relating to the acquisition or sale of interests in other companies or businesses which have been entered into within the last three years prior to the date hereof providing, in each case, for a consideration of EUR 100,000 or more;

ii) joint venture agreements, cooperation agreements, partnership agreements or similar agreements (other than the Constitutional Documents of the Company and the Subsidiaries);

iii) rental and lease agreements relating to assets or real estate which, individually, provide for annual payments of EUR 100,000 or more;

iv) loan agreements, bonds, notes or any other instruments of debt with an aggregate nominal amount of more than EUR 100,000 (excluding for the avoidance of doubt customary deferred payment arrangements with customers or suppliers);

v) guarantees, sureties (*Bürgschaften*), indemnities, letters of comfort (*Patronatserklärungen*) issued by any of the Company or either Subsidiary;

vi) agreements between the Company or either Subsidiary and any of the Sellers, relatives of any Seller or entities affiliated with any Seller or any of his relatives;

vii) any long-term agreement (*Dauerschuldverhältnis*) which cannot be terminated at will by the Company or the Subsidiary, as applicable, upon not more than 30 days prior notice, and which provides for annual obligations of the Company or the Subsidiary, as applicable, in excess of EUR 100,000 per year;

viii) any long-term agreement (*Dauerschuldverhältnis*) with customers, suppliers or agents (*Handelsvertreter*) which provides for annual obligations of the Company or any Subsidiary in excess of EUR 100,000 per year; or

ix) any agreement or arrangement to which the Company or either Subsidiary is a party which prevents the Company from competing in any part of the world.

7.5.2 To the Best Knowledge of the Sellers, unless otherwise disclosed in **Annex 7.5.2** to the Reference Deed, each Material Agreement is in full force and effect, neither the Company nor either Subsidiary is in default or breach under any such agreement and no party to a Material Agreement has given notice of termination or has threatened to terminate a Material Agreement.

7.5.3 No party to a Material Agreement has given notice of termination or has to the Best Knowledge of the Sellers threatened to terminate or vary a Material Agreement as a result of the transactions contemplated by this Agreement.

7.6 Employees; Pensions

7.6.1 **Annex 7.6.1** to the Reference Deed sets forth a true, correct and complete list of all persons employed by the Company and each Subsidiary.

7.6.2 There are no agreements with labor unions (*Gewerkschaften*), work councils agents (*Betriebsräte*) or other labor group arrangements by which any entity of the Company or either Subsidiary is bound. Except for the Company's obligations under the Plan, there are no material written commitments, and to the Sellers' Best Knowledge there are no material commitments of any kind, towards the workforce by which the Company is bound. The Company is in full compliance with its obligations under the Plan, except for instances of minor non-compliance which, in the aggregate, are not material to the Company.

7.6.3 The Sellers are not aware that any employee of the Company or either Subsidiary has plans to terminate his or her employment relationship with the Company or such Subsidiary, as applicable. None of the employees of the Company or either Subsidiary is represented by any labor union, and there is no labor strike or other labor trouble pending or, to the Sellers' Best Knowledge, threatened. No employee of the Company or either Subsidiary is, to the Sellers' Best Knowledge, obligated under any contract or subject to any judgment, decree or administrative order that would conflict or interfere with the performance of the employee's duties as an employee.

7.6.4 There are no (i) independent contractors who are hired directly and not through an agency or subcontracting company and who, to the Sellers' Best Knowledge, spend the majority of their working time on the business of the Company or either Subsidiary and (ii) persons to whom an offer of employment is made and accepted or outstanding.

7.6.5 All labor agreements of the Company's and both Subsidiaries' former employees were legally terminated and the Sellers are not aware of any circumstances that could give raise to adverse claims regarding labor issues.

7.7 **Insurance. Annex 7.7** to the Reference Deed contains a true and complete list of all material liability insurance contracts that insure the business, operations or affairs of the Company and both Subsidiaries, or affect or relate to the ownership, use or operations of any of their respective assets (the "**Business Insurances**"), all of which are in full force and effect. There are no claims currently pending or, to the Sellers' Best Knowledge, any basis therefore or threat thereof against the Company or either Subsidiary under any of the Business Insurances. The Company and each Subsidiary has materially satisfied its obligations under the Business Insurances.

7.8 **Litigation Matters and Proceedings before Governmental Authorities**. **Annex 7.8** to the Reference Deed contains a correct and complete list of all litigation matters and proceedings before courts and governmental authorities as well as arbitration panels in respect of which the Company or either Subsidiary is a party. The Sellers warrant that, to the Best Knowledge of the Sellers, there is no adverse claim from any third party, either formally served or otherwise, that is likely or possibly to result in litigations involving the Company or either Subsidiary.

7.9 **Solvency.** No insolvency proceedings (or similar proceedings under applicable laws) have been applied for regarding the assets of the Sellers, the Company or the Subsidiaries and there are no circumstances which would require or justify the opening of or application for such proceedings.

7.10 **Financial Statements**

7.10.1 The existing consolidated financial statements of the Company and the Subsidiaries for the business years 2009-2011, copies of which have been provided to the Purchaser prior to the notarization, (the "**Financial Statements**") have been prepared in accordance with the German generally accepted accounting principles set forth in the provisions of the HGB and provide a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the Subsidiaries at the respective date of statement. Sufficient provisions have been included and value adjustments have been carried out in the Financial Statements for all risks and uncertainties so far under applicable law required.

7.10.2 The Financial Statements are not adversely affected by any extraordinary or non-recurring items unless otherwise expressly stated therein.

7.10.3 As of December 31, 2011, neither the Company nor any Subsidiary was subject to any liabilities or obligations other than those listed in the Financial Statements, except for liabilities not required to be recorded under HGB that, in the aggregate, do not exceed EUR 100,000.

7.10.4 The books and records of the Company and the Subsidiaries are up-to-date and have been maintained materially in accordance with all applicable legal requirements and contain complete and accurate

records of all matters to be dealt with in such books under applicable law.

7.10.5 Since the last balance sheet day, except for liabilities and obligations incurred in the ordinary course of business and consistent with past practice, neither the Company nor any Subsidiary has incurred or agreed to assume or incur any material liabilities or obligations (whether direct, indirect, accrued or contingent).

7.11 Intellectual Property Rights

7.11.1 "**Intellectual Property**" shall mean all registered and unregistered intangible assets, including without limitation, utility models, trademarks, trade names, service marks, copyrights, design rights, any application thereof and know-how. "**Company Intellectual Property**" shall mean any and all Intellectual Property that is owned by or licensed to the Company or either Subsidiary. "**Registered Intellectual Property**" means Intellectual Property that is the subject of an application, certificate, filing, registration or other document issued by, filed with, or recorded by, any government or other public legal authority at any time in any jurisdiction. "**Open Source Materials**" shall mean any "open source", "public source" or "freeware" software, materials, or other technology, including any software licensed pursuant to any GNU general public license, lesser general public license, Mozilla public license, or a similar license.

7.11.2 The Company Intellectual Property owned by the Company is valid and enforceable. The Company Intellectual Property licensed to the Company is to the Best Knowledge of the Sellers valid and enforceable. The Company owns or is the licensee of the Company Intellectual Property. To the Best Knowledge of the Sellers there are no third parties that claim to own or to have an exclusive license to any Company Intellectual Property. The Company does not own, and has not applied for, any patents.

7.11.3 Except for the Company Intellectual Property listed in **Annex 7.11.3** to the Reference Deed the Company may transfer, or license the Company Intellectual Property without restriction or payment to a third party. The Company is not obligated to transfer or license any Company Intellectual Property, or any Intellectual Property Rights later developed or obtained by the Company, to a third party.

7.11.4 **Annex 7.11.4** to the Reference Deed lists (i) all Registered Intellectual Property owned by, filed in the name of, applied for by, or subject to a valid obligation of assignment to the Company; (ii) all third parties that share rights to such Registered Intellectual Property with the Company, including without limitation joint owners and co-applicants; and (iii) all actions that must be taken by the Company within 120 days of the

Closing Date to maintain the validity or enforceability of its Registered Intellectual Property.

7.11.5 The Company has sufficient rights to all Intellectual Property used in or necessary for the conduct of the Company's business as it currently is conducted by the Company with the qualification that, to the Best Knowledge of the Sellers, the conduct of the Company's business does not misappropriate, or otherwise violate the Intellectual Property of a third party in any way.

7.11.6 To the Best Knowledge of the Sellers there is no infringement, misappropriation, unauthorized use or violation of the Company Intellectual Property by any third party.

7.11.7 Apart from what has been disclosed in Annex 7.8 there is no pending (*rechtshängig*) litigation disputes regarding any license of Intellectual Property to or from the Company and to the Best Knowledge of the Seller no such litigation has been threatened against the Company.

7.11.8 The Company has not disclosed, delivered or licensed to any person or agreed or obligated itself to disclose, deliver or license to any person, or expressly permitted the disclosure or delivery to any escrow agent or other person of, any Company source code, other than disclosures to employees and consultants involved in the development of Company products.

7.11.9 **Annex 7.11.9** to the Reference Deed identifies all Open Source Materials used in any Company products, and indicates whether such Open Source Materials were modified and/or distributed by the Company and identifies the licenses under which such Open Source Materials were used. To the Best Knowledge of the Sellers the Company is materially in compliance with the material terms and conditions of all licenses for the Open Source Materials. To the Best Knowledge of the Sellers the Company has not (i) incorporated Open Source Materials into, or combined Open Source Materials with, the Company products; (ii) distributed Open Source Materials in conjunction with any Company products; or (iii) used Open Source Materials in such a way that, with respect to (i), (ii), or (iii), creates, or purports to create obligations for the Company that the Company products incorporated into, derived from or distributed with such Open Source Materials be (A) disclosed or distributed in source code form, (B) licensed for the purpose of making derivative works at no charge, or (C) redistributable at no charge.

7.11.10 All employees of the Company at any time involved in the creation of Intellectual Property for the Company have executed a proprietary information, confidentiality and invention assignment Contract substantially in the form made available to the Purchaser. Neither the Sellers nor any employee of, or freelancer who has worked for, the

Company or either Subsidiary is entitled to or has claimed any payment or compensation in respect of Intellectual Property Rights and/or its use in the business of the Company or either Subsidiary (including without limitation compensation according to the German Employee Inventions Act). Service inventions (*Diensterfindungen*) which are part of Intellectual Property and achieved by German employees, have been claimed in compliance with Section 5 of the German Employee Invention Act (*Arbeitnehmererfindungsgesetz*).

7.11.11 The Company is in compliance with all material German applicable laws and its internal privacy policy relating to the privacy of users of its products and services.

7.11.12 Except as set forth in **Annex 7.11.12**, to the Reference Deed no government funding, facilities or resources of a university, college, other educational institution or research center or funding from third parties was used in the development of the Company's Intellectual Property, and no respective governmental entity, university, college, other educational institution or research center referred to in Annex 7.11.12 has any claim or right in or to such Company Intellectual Property.

7.12 Tax/Taxes

7.12.1 "Tax" or "Taxes" shall mean

i) a payment which is levied by or on behalf of a German or non-German public body to raise income ("**Tax Authority**"), including taxes within the meaning of section 3 par. 1 of the German General Fiscal Code (*Abgabenordnung*) or any corresponding foreign legal regulations including administrative fines as well as interest, costs and surcharges or any other additional costs within the meaning of section 3 par. 4 of the German General Fiscal Code (*Steuerliche Nebenleistungen*) in respect of the Company and each Subsidiary, social security contributions and customs and excise duties (*Zölle*), taxes deducted at source and withholding taxes which the Company or any Subsidiary has to withhold and pay from payments to third parties without itself being a person liable to pay tax as well as payments from tax allotment agreements or comparable agreements, and any similar charges, duties or fees imposed by any public authority or governmental body (such as subsidies), each in respect of the Company and each Subsidiary.

ii) any of the payments listed under sub-paragraph (i) above, imposed on the Company as a secondary liability (*Haftungsschuld*);

regardless of how and by whom such payment is collected and whether it is owed jointly and/or severally.

7.12.2 Filings and Payments. Except as set forth in **Annex 7.12.2** to the Reference Deed:

i) All returns, documents, declarations, filings, notifications and information which the Company or either Subsidiary has made or provided for Tax purposes have been filed in good time, have been properly prepared in accordance with all applicable laws or common practice, with all regulations and any agreement or arrangement made with any competent Tax Authority and have been validly and timely made or provided to the appropriate Tax Authority. All such information that the Company or either Subsidiary has at any time supplied to any Tax Authority has been complete and true in all material respects;

ii) The Company and each Subsidiary has at all times punctually paid all Tax that has become due on or before the Closing Date;

iii) To the extent that any Tax has not yet been due at the statement day of the Financial Statement for the business year 2011, they have been accrued in the balance sheets being part of the Financial Statement for the business year 2011 except for the amount which has been discussed and disclosed between the Parties within the tax due diligence and which has been accrued in 2012 prior to the Closing Date, as reflected in the interim accounts as per 15 November 2012 which is attached hereto as **Annex 7.12.2iii)**, it being understood that the Tax not yet due (but accrued for in the Financial Statement 2011 and in the interim accounts as per 15 November 2012) shall not exceed an aggregate sum of EUR 123,300;

iv) All records and documentation, especially with respect to transfer pricing which the Company and each Subsidiary is required to keep for Tax purposes or which would be needed to substantiate any claim made or position taken in relation to Tax by the Company and each such Subsidiary, have been duly kept and are available for inspection at the premises of the Company and the Subsidiary if and to the extent the Company was obliged to keep such records by statutory law;

v) No binding ruling or other decision of a Tax Authority has been issued towards the Company or any Subsidiary which would in future impair, limit or otherwise influence the conduct of business or a reorganization of the Company or either Subsidiary.

7.12.3 There is no ongoing audit, review material, disagreement or dispute between the Company and any Tax Authority with regard to any returns or otherwise in connection with Tax and neither the Company nor either Subsidiary is, or has been the subject of an investigation (other than regular routine inquiries or tax audits) by any Tax Authority.

7.12.4 The Company is and has always been exclusively resident in Germany for tax purposes. *eleven-internationale Vertriebsgesellschaft mbH* is and has always been exclusively resident in Germany for tax purposes. *eleven USA Inc.* has always been exclusively resident in Delaware and/or California, U.S.A, for tax purposes;

7.12.5 To Sellers' Best Knowledge no transaction in the Company or any Subsidiary with its shareholder or any other related party qualifies taxwise as hidden distribution of profits/constructive dividends (*verdeckte Gewinnausschüttung*) and those transactions have been set-up in accordance to arm's length standards. Transactions directly related to this Agreement are not part of this Section.

7.12.6 Neither the Company nor either Subsidiary has transferred assets to a company or partnership in a tax exempt reorganization, including without limitation, any transaction referred to in sec. 6 para. 5 sent. 3 of the Income Tax Act or sec. 20 Reorganisation Tax Act (*Umwandlungssteuergesetz*).

7.12.7 Neither the Company nor either Subsidiary has claimed a deduction for a write down of any of its assets with tax effect without the course of scheduled depreciation or amortization unless fully recaptured prior to Closing or set forth in **Annex 7.12.7** to the Reference Deed.

7.12.8 Any wage taxes and social contribution payments in relation to the settlement of the Plan have been or will be paid in time when due on or before Closing.

With respect to any claims related to tax guarantees pursuant to this Sec. 7.12, Sec. 9 shall apply accordingly.

7.13 **Public Grants**. There are no public investment grants (*Investitionszulagen*) or investment subsidies (*Investitionszuschüsse*) and any other public or private subsidy or grant which has not been disclosed to the Purchaser and which will have to be repaid as a result of the consummation of the transactions reflected in this Agreement nor due to other circumstances.

7.14 **Permits.** The Company and each Subsidiary holds all permits and required licenses necessary for their present operations and no revocation of any such permit is impending.

7.15 **Leased Real Estate. Annex 7.15** to the Reference Deed includes a correct and complete list of all real estate leased by the Company or either Subsidiary from any third party and correctly states for each such piece of real estate the location,

size and use, the landlord and the date of the lease agreement (the "**Leased Real Estate**"). No real estate other than the Leased Real Estate is currently used by or necessary for the Company and each Subsidiary to conduct its business as conducted on the Closing Date.

7.16 **No conflict**. Except for the Material Contracts listed in **Annex 7.16** to the Reference Deed to the Best Knowledge of the Sellers, the execution and delivery by the Company and the Sellers of this Agreement, and the consummation of the Transaction, will not conflict with or result in any violation of or default under (with or without notice or lapse of time, or both) or give rise to a right of termination or cancellation, modification or acceleration of any obligation or loss of any benefit under (any such event, a "**Conflict**") any material contract to which the Company is a party or by which any of its properties or assets are bound. **Annex 7.16** of this Agreement sets forth all necessary consents, approvals, notices, waivers or declarations of parties to any material contracts to which the Company is a party, as are required thereunder in connection with the Transaction, or for any such contract to remain in full force and effect immediately after the Closing.

7.17 **No right out of the Transaction**. Neither the Company nor either Subsidiary has any obligation or liability to pay any fees or commissions to any broker, finder, agent or any third person in relation to the consummation of the transaction contemplated by this Agreement. No third party including without limitation employees, managers and other parties of agreements can claim any payments or exercise rights against / towards the Company or either Subsidiary in relation to the consummation of the transaction contemplated by this Agreement.

7.18 **Securities Law**

7.18.1 Each Seller is not a U.S. Person as defined in Regulation S (a "**Regulation S Investor**") promulgated under the Securities Act of 1933, as amended (the "**Securities Act**") by the United States Securities and Exchange Commission (the "**SEC**"). If such Seller is a Regulation S Investor, such Seller also represents that: (1) it is not a U.S. Person, (2) it was not organized under the laws of any United States jurisdiction, and was not formed for the purpose of investing in securities not registered under the Securities Act, (3) on the date of this Agreement, the Regulation S Investor is outside the United States, (4) the Seller is not acquiring the Equity Consideration for the account or benefit of any U.S. Person, (5) it will not, during the one-year period starting on the date of such Seller's purchase and receipt of the Equity Consideration, offer or sell any of the Equity Consideration (or create or maintain any derivative position equivalent thereto) in the United States, to or for the account or benefit of a U.S. Person other than in accordance with Regulation S or pursuant to an effective registration statement under the Securities Act or any available exemption therefrom and, in any case, in accordance with applicable state securities laws, (6) it will, after the expiration of such one-year period,

offer, sell, pledge or otherwise transfer the Equity Consideration (or create or maintain any derivative position equivalent thereto) only pursuant to an effective registration statement under the Securities Act or any available exemption therefrom and, in any case, in accordance with applicable state securities laws and (7) that the offer and issuance of the Equity Consideration to such Seller was made in an offshore transaction (as defined in Rule 902(h) of Regulation S), no directed selling efforts (as defined in Rule 902(c) of Regulation S) were made in the United States, and such Seller is not acquiring the Equity Consideration for the account or benefit of any U.S. Person.

7.18.2 Each Seller has confirmed on the signature page hereto whether such Seller is a Regulation S Investor. Each Seller represents and warrants that the information set forth on its respective signature page is true and correct.

7.18.3 Such Seller understands that, in connection with the acquisition of the Equity Consideration as contemplated herein, the shares of the Equity Consideration have not been and will not be registered under the Securities Act or registered or qualified under the securities laws of any U.S. state or other jurisdiction, in each case by reason of specific exemptions from the registration provisions of the Securities Act and the securities laws of such states or other jurisdictions, the availability of which depend upon, among other things, the bona fide nature of the investment intent and the accuracy of such Seller's representations as expressed herein and in response to Purchaser's inquiries, if any. Moreover, such Seller understands that Purchaser is under no obligation to register the Equity Consideration with the SEC.

7.18.4 Such Seller understands that the Equity Consideration that such Seller is acquiring pursuant to this Agreement are and will be "restricted securities" under the Securities Act in that such securities will be acquired from Purchaser in a transaction not involving a public offering under the Securities Act, and that under U.S. federal and state laws and applicable regulations, such Equity Consideration may be resold without registration under the Securities Act only in certain limited circumstances and that otherwise such securities must be held indefinitely. In this connection, the Seller represents that it understands the resale limitations imposed by the Securities Act and is familiar with SEC Rule 144, as presently in effect, and the conditions which must be met in order for that rule to be available for resale of "restricted securities." Such Seller also acknowledges that such Seller may deemed to be an Affiliate of Purchaser and that, if so, certain resale limitations thereunder shall apply to such Seller for so long as such Seller remains an Affiliate and for three months thereafter.

7.18.5 Such Seller has received and reviewed information about Purchaser, including the reports filed by Purchaser with the SEC, and has had an opportunity to discuss Purchaser's business, management and financial affairs with its management. Such Seller is aware of Purchaser's business affairs and financial condition and has acquired sufficient information about Purchaser to reach an informed and knowledgeable decision to acquire the Equity Consideration.

7.18.6 Such Seller acknowledges that Purchaser has informed such Seller that the market value of the Equity Consideration shall be as specified in Section 3.2.2.1 above.

7.18.7 Such Seller acknowledges that at no time was such Seller presented with or solicited by any publicly issued or circulated newspaper, mail, radio, television or other form of general advertising or solicitation in connection with the offer, sale and purchase of the Equity Consideration.

7.18.8 Such Seller acknowledges that such Seller is fully aware of: (a) the speculative nature of the Equity Consideration; and (b) the qualifications and backgrounds of the management of Purchaser.

7.18.9 Such Seller has had an opportunity to review with his own Tax advisors the Tax consequences to him of the transactions contemplated by this Agreement, including the receipt of Equity Consideration. Such Seller understands that such Seller must rely solely on his advisors and not on any statements or representations by Purchaser, the Company or any of their attorneys, investment advisors, accountants or other agents with respect to Tax matters.

Such Seller acknowledges that such Seller either alone or with his purchaser representative(s), has such knowledge and experience in financial and business matters that such Seller is capable of evaluating the merits and risks of the share purchase, has the capacity to protect such Seller's own interests in connection with this transaction and is financially capable of bearing a total loss of the Equity Consideration.

7.19 **No Untrue Statement**. The information provided in connection with this Transaction to the Purchaser is accurate in all material respects, is not misleading and, to the Best Knowledge of the Sellers, does not omit anything material relating to the Company or the Subsidiaries which the Purchaser should be aware of in order to be able to evaluate such information. To the Best Knowledge of the Sellers there are no material facts or circumstances which in the future could have a materially adverse effect on the Company or its Subsidiaries except for general developments of the economy or the market.

8 Remedies

8.1 The representations and warranties of the Sellers set forth in Section 7 of this Agreement shall survive the Closing for a period of 12 months thereafter; *provided, however*, (i) that in the event of fraud, willful breach or intentional misrepresentation of a representation or warranty, such representation or warranty shall survive until the expiration of the applicable statute of limitations; (ii) the representations and warranties of the Sellers set forth in **Section 7.2** (*Status of the Company*) and **Section 7.11.2** through **Section 7.11.5** (*Intellectual Property Rights*) shall survive the Closing for a period of 3 years thereafter; and (iii) the representations and warranties set forth in **Section 7.3** (*Status of Sellers and Shares*) shall survive the Closing for a period of 5 years thereafter. **Sections 8.1(i), 8.1(ii)** and **8.1(iii)** above are referred to herein as "**Extraordinary Claims**". The agreements, covenants and other obligations of the parties hereto shall survive the Closing in accordance with their respective terms. The dates on which the applicable survival periods referenced in this **Section 8.1** expire shall be referred to, collectively, as the "**Expiration Dates**" and the date on which each applicable survival period expires shall be referred to as the "**Applicable Expiration Date**".

8.2 If one or more of the representations or warranties of the Sellers set forth in Section 7 are incorrect, incomplete or not complied with (the "**Breach of Guarantee**"), the Purchaser may demand from the Sellers, jointly and severally (except that in the case of a Breach of Guarantee relating to a representation and warranty made by a Seller as to himself or as to his specific Shares, the liability shall be (i) several and not joint and (ii) a Seller shall not bear liability greater than the gross amount received by him under this Agreement with respect to his Shares (it being understood that amounts not yet received but receivable in the future may further be offset by the Purchaser against warranty claims provided they do not lead to a payment obligation of the respective Seller beyond the gross amount received by him), except that there shall be no limitation on the liability of any Seller who commits fraud, to put it in the position in which it would have been if the respective guarantee had been correct (*restitution in kind - Naturalrestitution*), within a period of three months following receipt of a corresponding demand in writing from the Purchaser. If the respective Seller does not put the Purchaser in the guaranteed position within the time limit set, the Purchaser shall be entitled to demand monetary compensation from the respective Seller for the resulting losses from the Breach of Guarantee. The same is the case if and to the extent that restitution in kind is impossible or cannot be effected by Sellers with reasonable efforts.

8.3 Only if Seller fails to comply with his obligations under Section 8.2, Purchaser may, at its discretion, claim (i) specific performance of such obligations or (ii) payment of monetary damages (*Schadensersatz in Geld*). The obligation to pay monetary compensation is limited to the actual and direct damages incurred by the Purchaser but shall include costs for reasonable recovery including for experts and in any event include the amount which Purchaser would dedicate in

order to put himself and/or the Company in the position as if the guarantee would have been correct. Particularly, further indirect or consequential damages (*Mangelfolgeschäden*), loss of profits, internal management costs or frustrated expenses shall not be compensated. The legal principles as to the calculation of damages, mitigation of damages and offsetting of losses by advantages due to the damaging event pursuant to Sec. 249 et seq. of the German Civil Code (BGB) shall apply to all claims of Purchaser under or in connection with this Agreement. Compensation must be paid to the Purchaser or, at the request of same, to the Company.

8.4 Notwithstanding anything to the contrary contained in this Agreement, the maximum liability of any Seller for such monetary damages shall be the Escrow Fund (the "**General Indemnification Cap**") except that indemnification for monetary damages as a result of, arising out of or in connection with Extraordinary Claims shall not be subject to the General Indemnification Cap but shall be limited, in the aggregate to the Initial Purchase Price actually received by an Indemnifying Party hereunder on a pro rata basis (it being understood that amounts not yet received but receivable in the future may further be offset by the Purchaser against warranty claims provided they do not lead to a payment obligation of the respective Seller beyond the gross amount received by him), except that there shall be no limitation on the liability of any Seller who commits fraud.

8.5 Sellers shall only be liable for Breach of Guarantee if (i) the amount recoverable with respect to the individual Claim made exceeds EUR 40,000 (in words: Euro forty thousand); and (ii) the aggregate amount recoverable with regard to all claims made exceeds an amount of EUR 80,000 (in words: Euro eighty thousand); if either of the Euro thresholds in the foregoing sentence is exceeded, the Purchaser shall be entitled to receive the entire such amount from the first Euro of loss as if such threshold did not exist.

8.6 Any monetary damages recoverable by the Purchaser from the Sellers pursuant to this Section 8 shall first be recovered by reduction of the recovered amount from the respective pro rata portion of such Seller in the Escrow Fund, and only after such amount is depleted, may the Purchaser recover any remaining amount (if and to the extent the Purchaser is entitled to recover from the Seller(s) for monetary damages in excess of the Escrow Fund pursuant to this Section 8 directly from such Seller(s)). Any representation and warranty of Sellers in Section 7 above which refers to the "**Best Knowledge of the Sellers**" is only breached if Seller 1 had either actual knowledge of the relevant fact or grossly negligently (*grob fahrlässig*) could have information of the relevant fact if he had used the diligence of a prudent businessman pursuant to § 43 Limited Liability Companies Act *(GmbHG*).

8.7 Procedure in respect of Purchaser's claims in general:

8.7.1 In the event that the Purchaser becomes aware of a Breach of Guarantee prior to the Applicable Expiration Date, it shall promptly

deliver a certificate (a "**Claim Certificate**") to the Representative, specifying all relevant facts resulting in the Purchaser's claim under this Agreement.

8.7.2 In the event that any such matter is related to any claim or proceeding asserted or commenced by any third party including any governmental authority (a "**Third Party Claim**"), Seller 1 shall have the right, at any time, at its cost to assume the control of the defense of the Third Party Claim. In particular, Seller 1 may select counsel and instruct the Purchaser to litigate or settle, or cause to be litigated or settled, the Third Party Claim in accordance with Seller 1's instructions. The Purchaser shall assist, at Seller 1's cost and expense, the Seller in the defense of any Third Party Claim (internal costs not being chargeable). Such assistance shall include, without limitation, the providing and making available to Seller 1 of all books, records and other information, and of all managing directors and employees of the Purchaser, its affiliates or the Company, to the extent necessary or useful in connection with the defense of Third Party Claim unless this is against the economic or financial interest of the Purchaser and/or the Company. Costs and expenses incurred by Sellers in defending any Third Party Claims in accordance with the foregoing provisions shall be borne by the Sellers. Any failure of the Purchaser to comply with any of its obligations regarding Third Party Claim under this Section shall release the Sellers from their respective obligation under this Agreement, except if (and to the extent that) the Sellers are not prejudiced by such failure. Purchaser may chose to waive the respective against Sellers under this Section 8 if compliance with this Section 8.7.2 would according to its free judgment infringe its economic interests.

8.7.3 In case of a Third Party Claim arising which could lead to a breach of warranties pursuant to Section 7.11 (Intellectual Property Rights), the Parties are obliged to jointly defend the Third Party Claim at Commtouch's expense. Purchaser's and Commtouch's obligations regarding access to information provided for in Section 8.7.3 shall apply *mutatis mutandis*.

8.7.4 In the event that any such matter does not relate to a Third Party Claim, the Representative shall have 20 Business Days following his receipt of a Claim Certificate to object to any item(s) or amount(s) set forth therein by delivering written notice thereof (an "**Objection Notice**") to Purchaser, with a copy to the Escrow Agent (if and to the extent that the Purchaser is seeking recourse against the Escrow Fund in accordance with Section 8.1). In the event that the Representative shall fail to object, to any item or amount set forth in a Claim Certificate as set forth herein, the Representative shall be deemed to have

agreed and consented (for and on behalf of the Sellers) to each such item and amount set forth in the Claim Certificate ("**Deemed Losses**"). Upon the expiration of such 20 Business Day period, if the claim set forth in the Claim Certificate is in whole or in part against the Escrow Fund and if the Representative failed to object as stipulated above, Purchaser shall be entitled to deliver to the Escrow Agent (with a copy to the Representative) instructions requiring the Escrow Agent to promptly release from the Escrow Fund and deliver to Purchaser an amount of cash equal to any Deemed Losses.

8.7.5 In the event that the Representative delivers an Objection Certificate as set forth herein, the Representative and Purchaser shall attempt in good faith to agree upon the rights of the respective parties with respect to each of such claims objected to in such Objection Certificate (the "**Agreed Losses**"). If the Purchaser and the Representative should so agree, a memorandum setting forth such agreement with respect to the Agreed Losses shall be prepared and signed by both parties and furnished to the Escrow Agent who shall deliver to Purchaser an amount of cash equal to any Agreed Losses.

8.7.6 Should Purchaser and the Representative be unable to agree as to any particular item or items or amount or amounts specified in an Objection Certificate within the time periods specified above, then the matter shall be settled by an arbitrator agreed upon by the Parties and such decision shall be final, binding and conclusive upon the Sellers (the "**Awarded Losses**"). Any ruling or decision of the arbitrator may be enforced in any court of competent jurisdiction. Purchaser shall provide the Escrow Agent with the written resolution of the arbitrator to distribute to Purchaser, out of the Escrow Fund, an amount equal to the Awarded Losses.

8.8 The Escrow Fund shall be held as a trust fund and shall not be subject to any Lien, attachment, trustee process or any other judicial process of any creditor of any party, and shall be held and disbursed solely for the purposes and in accordance with the terms of this Agreement and the Escrow Agreement.

8.9 Any amounts remaining in the Escrow Fund shall be released from the Escrow Fund on the date which is the 12 month anniversary of the Closing Date (the "**Escrow Release Date**") (less any portion of the Escrow Fund which is necessary to satisfy any unresolved claims specified in any Claim Certificate that has been properly delivered by the Purchaser prior to the Applicable Expiration Date and the Escrow Release Date (such amount, the "**Holdback Amount**")). On the Escrow Release Date, the Escrow Agent shall deliver to the Sellers on a pro rata basis the remaining portion of the Escrow Fund (less the Holdback Amount, if any) and shall retain the Holdback Amount, if any, in accordance with this **Section 8.9**. Upon resolution of any such unsatisfied or unresolved claim for Losses in accordance with any of the provisions of this Section 8, the Escrow

Agent shall release such portion of the Holdback Amount required to satisfy such claims, as soon as reasonably practicable.

8.10 The Purchaser shall forfeit its right to exercise its rights under or in connection with this Agreement in case the Purchaser, its accountants, legal advisors or any of its directors or employees was aware of the fact that a representation or warranty is untrue, incomplete or not complied with. The provisions of § 442 BGB, § 443 BGB and § 377 HGB shall not apply. Purchaser has in the course of its due diligence been provided with the documents in the data room listed in **Annex 8.10** to the Reference Deed. The parties have recorded the documents listed in Annex 8.10 to the Reference Deed on a DVD as data carrier. For documentary purposes, the parties have handed over to the acting notary such a data carrier with those recorded data and do thereby instruct him, to keep the data carrier together with the original (*Urschrift*) of this deed in his custody and to make, at the written request of any of the parties, a complete or partial copy available to, and at the expense of, the requesting party. The parties are aware of the fact that the notary has not reviewed the contents of the data carrier and does not assume any liability for the permanent accessibility of the data recorded on the data carrier. The acting notary is entitled to destroy the data carrier after expiry of two years of the notarization of this deed. Each Party will further be provided with a copy of this data room DVD at Closing.

8.11 To the extent permitted by law, rights and remedies of the Purchaser based on a Breach of Guarantee, in particular based on statutory warranty rights and warranties such as withdrawal from the agreement (*Rücktritt*), reduction of purchase price (*Minderung*), repair or compensation (*Nachbesserung*), culpa in contrahendo, adjustment or reversal of the Agreement due to frustration of the contract (*Wegfall der Geschäftsgrundlage*) as well as the contesting of the Agreement due to the absence of an essential characteristic (*Anfechtung wegen des Fehlens einer verkehrswesentlichen Eigenschaft*) are expressly excluded, except for rights and remedies of the Purchaser according to sections 123 BGB, 444 BGB, 823 BGB and 826 BGB as well as any rights based on wilful misconduct.

9 Tax Indemnities; Cooperation in Tax Matters

9.1 The Sellers agree to indemnify and hold harmless the Purchaser and/or the Company, completely and without delay, from and against all Taxes due and payable by the Company (and any other financial disadvantages directly related to such Taxes) for assessment periods ending on or before the Closing Date to the extent such Taxes (i) have not been reflected in the Financial Statements for the business year 2011, clearly specified as tax liabilities or as tax provisions, and (ii) have not been reflected as accruals in the interim accounts as per 15 November 2012 (Annex 7.12.2 iii), collectively: "**Additional Taxes**", except to the extent that such Additional Taxes

9.1.1 are caused by transactions carried out by the Purchaser, its affiliates or the Company after the Closing Date;

9.1.2 can be reclaimed by the Purchaser, its affiliates or the Company on the basis of an enforceable and valuable claim against any other third party ("**Claim**"); any additional costs of the Purchaser, its affiliates or the Company for demonstrating that the Claim is not valuable shall be reimbursed by the Sellers;

9.1.3 do result in a tax reduction or other tax benefits in assessment periods starting after the Closing Date ("**Tax Benefit**") provided that such tax benefit has been realized within five years after the Closing Date. If Additional Taxes have already been paid to Purchaser, Sellers can reclaim the amount of the Tax Benefit. In any case, the Tax Benefit needs to be discounted with a discount rate of 3% and a tax rate of 30%.

9.2 Claims under Section 9.1 also exist for Taxes which will be assessed for assessment periods starting before and ending after the Closing Date ("**Straddle Period**") and which shall be allocated to the Straddle Period ("**Allocation Principle**"):

9.2.1 Insofar the Taxes are triggered by extra-ordinary measures (e.g. constructive dividend, transfer of assets, restructuring) of the Sellers (except the settlement of the Plan) those Taxes qualify as Additional Taxes as if the assessment period would end on the Closing Date,

9.2.2 Insofar the Taxes are triggered by the settlement of the Plan 50% of those Taxes shall qualify as Additional Taxes and shall be indemnified by the Sellers;

9.2.3 In all other cases the Taxes for the whole Straddle Period multiplied by a fraction of the numerator of which is the number of days in the assessment period ending on the Closing Date and the denominator of which is the number of days of the whole Straddle Period.

Section 9.1 applies accordingly for all Additional Taxes under this Section 9.2.

9.3 If and to the extent the Company receives a refund of Taxes after the Closing Date for an assessment period ending on or before the Closing Date or for the Straddle Period ("**Tax Refund**") the Purchaser shall pay such amount to the Sellers pursuant to their shareholdings in the Company at Closing or off-set against any claims he has under this Section 9. In case of a Tax Refund for the Straddle Period the Allocation Principle of Section 9.2 shall apply accordingly for the Tax Refund.

9.4 Irrespective of the period of limitation for other claims under this Agreement, all claims under this Section shall prescribe six (6) months after the final and binding Tax Assessment (*bestandskräftig und unanfechtbar)* or any corresponding or similar event of the respective Tax. Furthermore, any other limitation for other claims under this Agreement (in particular but not limited to Section 8) shall not

apply to tax claims, including (but not limited to) tax claims under this Section and tax claims related to Section 7.12 .

9.5 Sellers shall make any payments under this Section 9 to the Purchaser or, upon the Purchaser's discretion to the Company or its Subsidiaries, within twenty [***20***] business days after notice and presentation of a copy of the respective Tax assessment. Purchaser shall make any payments under this Section 9 to the Sellers within twenty [20] business days after notice of a Tax Refund.

9.6 Any payment made by the Sellers under this Section 9 is considered to be a reduction of the Initial Purchase Price, unless prohibited by mandatory statutory law. Any payment made by the Purchaser under this Section 9 is considered to be an increase of the Initial Purchase Price, unless prohibited by mandatory statutory law.

9.7 Cooperation in Case of a Tax Procedure/Tax Dispute

9.7.1 If a claim arises as a result of or in connection with a liability or alleged liability to any Tax Authority, especially a tax field audit, litigation or other procedure, for the period ending on or before the Closing Date ("**Tax Procedure**"), then, in addition to the obligations provided for in this clause,

i) the Purchaser shall, after it is informed by an official notice of a Tax Authority of a Tax Procedure concerning the Company, immediately and without undue delay give notice in writing to the Representative, including copies of the Tax Authority's notice, if in writing, or other documents received together with the notice;

ii) the Sellers may request the Purchaser to dispute, resist, appeal, compromise or defend the Claim and any adjudication in respect thereof and that any comments of the Sellers are duly incorporated into any statements to the Tax Authorities, unless such comments are in violation of applicable statutory laws or unreasonable ("**Tax Dispute**");

iii) the Purchaser shall, and shall procure that the Company shall, permit the Representative or its duly authorized advisors, if they are subject to a professional duty of confidentiality, to be involved in the Tax Procedure/Tax Dispute and to participate in meetings, discussions and correspondence with the Tax Authorities, including any final meetings with a Tax auditor, if reasonable;

iv) the Purchaser shall, and shall procure that the Company shall, give full information and full access to the books and records of the Company to the extent that they relate to the fiscal periods ending on or before the Closing Date and are relevant for the claim.

9.7.2 All expenses and costs at the level of Purchaser and/or the Company that arise and are directly born in connection with any Tax Dispute and that are not unreasonably caused, shall be borne by the Sellers pro rata.

9.8 Procedures in Relation to the Preparation of Tax Returns etc.

If Tax Returns in the name of the Company have to be prepared after the Closing Date relating to any period ending on or before the Closing Date, such Tax Returns shall be prepared by the Representative but reviewed and filed by the Company in accordance with the following:

9.8.1 The Purchaser shall procure that the Representative is given full information and full access to the books and records of the Company to the extent that they relate to periods ending on or before the Closing Date and are relevant for the Tax Return;

9.8.2 The Representative shall prepare the respective Tax Return on a basis consistent with those for prior assessment periods;

9.8.3 The Purchaser and the Company shall receive a copy of the prepared Tax Return at least twenty-five (25) Business Days prior to the due date of the respective Tax Return.

9.8.4 The Purchaser undertakes to consult with the Representative and to attempt in good faith to resolve any dispute between the Representative and the Purchaser in relation to the Tax Return.

10 Conduct Prior To The Closing

During the period from the date of this Agreement and continuing until the earlier of the termination of this Agreement or the Closing, the Sellers agree that they shall cause the Company to operate its business in the ordinary course consistent with past practices of the Company, except (a) with the prior written consent of Purchaser (the decision with respect to which will not be unreasonably delayed) or (b) as specifically contemplated by this Agreement. The Sellers shall cause the Company to pay indebtedness for borrowed money and Taxes of the Company in the ordinary course of business when due (subject to the right of Purchaser to review and approve any Tax Returns filed on or prior to the Closing), to use reasonable efforts to (i) pay or perform other obligations when due, (ii) to the extent consistent therewith, to preserve intact the present business organizations of the Company, (iii) keep available the services of the present officers and employees of the Company, and (iv) preserve the Company's assets and technology and preserve the relationships of the Company with material customers, suppliers, distributors, licensors, licensees, and others having business dealings with them, all with the goal of preserving unimpaired the goodwill and ongoing business of the Company at the Closing. Without limiting the foregoing, during the period from the date of this Agreement and continuing until the earlier of the termination of this Agreement or the Closing, except as set forth in clauses (a) through (b) of the first sentence of this Section 10, the Sellers shall take all measures necessary to ensure that the Company shall not (i) amend its

Constitutional Documents, (ii) issue, sell or grant any share capital or other equity interest, (iii) issue, sell or grant, or authorize or propose the issuance, sale or grant of any options, warrants, call rights, convertible securities, commitments or agreements of any character, written or oral, to issue, deliver, sell, or cause to be issued, delivered or sold, any Share Capital or other equity interest, (iv) declare, set aside or pay any dividend or any other distribution payable in cash, stock or property or redeem, purchase or otherwise acquire directly or indirectly any of the Shares, (v) split, combine or reclassify any of the Shares, (vi) enter into any new, or amend, terminate or renew any contract or agreement that is or would be a Material Agreement, (vii) enter into any new, amend, terminate or renew any existing, employment, severance, consulting or salary continuation agreements, the Plan or any similar plan if in effect as of the date hereof, with or for the benefit of any employee, or engage any employee or consultant or service provider, (viii) grant any increases in the compensation, perquisites or benefits (whether through the payment of, or agreement to pay, bonus amounts or otherwise) to any Employee, (ix) create any new liabilities of any kind, (x) take any action that would result in any of the Conditions Precedent in Section 6 not being satisfied or that would delay their satisfaction, (xi) authorize the entrance into, or enter into any contract to do any of the foregoing. The Sellers shall promptly notify Purchaser of any material event involving the Company that arises during the period from the date of this Agreement and continuing until the earlier of the termination date of this Agreement or the Closing.

11 Confidentiality, Announcements and Press Releases

11.1 Each of the Sellers and the Purchaser hereby agree that they will not, at any time hereafter, divulge to any third party (other than in accordance with the provisions of this Section 11) any information relating to the Sellers (in the case of the obligation owed by the Purchaser) or the Purchaser (in the case of the obligation owed by the Sellers) that the relevant Party has obtained from the other by virtue of its consideration and negotiation of the Transaction, between 19 April 2012 and the Closing Date, other than as specifically permitted by the confidentiality agreement between the Sellers' advisor and the Purchaser dated 19 April 2012.

11.2 No announcement or statement about this Agreement or the subject matter of, or any matter referred to in, this Agreement (including, if applicable, the termination of this Agreement and the reasons therefore) shall be made or issued before, on or after the date of the Closing by or on behalf of either Party without the prior written approval of the other Party, provided that (i) nothing shall restrict the making by the Purchaser of any statement or disclosure which may be required by any applicable law or the rules of a recognized stock exchange upon which securities of the Purchaser (or a member of the group of which it is part) are traded or listed so long as the Company shall have received notice (and a copy) of the disclosure at least 24 hours prior to it being made, if feasible; and (ii) the parties shall issue a joint press release to announce the Transaction at such time as shall be mutually agreed upon by the Parties.

12 Expenses

Whether or not the Transaction is consummated, all Transaction Fees shall be the obligation of the respective Party incurring such fees and expenses, and all Transaction Fees of the Company shall be the obligation of the Sellers. "**Transaction Fees**" shall mean all fees and expenses incurred by a Party in connection with this Agreement or the transactions contemplated hereby, whether or not paid or payable prior or subsequent to the Closing, including: (a) all legal, accounting, tax, financial advisory, consulting and all other fees and expenses of third parties incurred by a Party in connection with the negotiation of the terms and conditions of this Agreement and the consummation of the transactions contemplated hereby; and (b) any brokerage or finders' fee, agents' commission or any similar charge in connection with the Transactions contemplated by this Agreement. Notary and registration costs shall be paid by the Purchaser.

13 Disputes

13.1 All disputes arising out of or in connection with this Agreement (including without limitation, claims for set-off or counter-claim) or its validity shall firstly be referred to the [Chief Executive Officers/Managing Director] of the Purchaser and the Representative, who shall enter into discussions in an attempt to reach a mutually satisfactory agreement in relation to them.

13.2 If the Chief Executive Officers/Managing Directors have not reached agreement by the end of the 20th Business Day on which such referral has been made to them, then the shall be finally settled by three arbitrators in accordance with the Arbitration Rules of the German Institution of Arbitration e.V. (DIS) without recourse to the ordinary courts of law. The venue of the arbitration shall be Frankfurt am Main. The language of the arbitration proceedings shall be English. This arbitration clause shall be governed by the substantive laws of the Federal Republic of Germany.

13.3 Nothing contained in this Agreement shall preclude any Party from seeking injunctive or other equitable relief from a court of law having appropriate jurisdiction.

14 Representative

14.1 The Sellers, by approving this Agreement and the transactions contemplated hereby, irrevocably appoint and constitute Mr. Robert Rothe as the Representative for and on behalf of the Sellers to execute and deliver this Agreement and the Escrow Agreement and for all other purposes hereunder and thereunder, to give and receive notices and communications, to take all actions and to authorize all actions on behalf of the Sellers under this Agreement and the Escrow Agreement as fully as though such actions were taken by the Sellers

themselves. Sellers entitled to a majority of the Initial Purchase Price may replace the Representative from time to time upon not less than ten (10) days' prior written notice to the Purchaser and the escrow agent under the Escrow Agreement. The Representative shall receive no compensation for his services. Notices or communications to or from the Representative shall constitute notice to or from each of the Sellers.

14.2 The Representative shall not be liable for any act done or omitted hereunder as Representative while acting in good faith and any act done or omitted pursuant to the advice of counsel shall be conclusive evidence of such good faith. The Sellers shall severally and pro rata indemnify the Representative and hold him harmless against any loss, liability, expense or fee incurred without gross negligence or bad faith on the part of the Representative and arising out of or in connection with the acceptance or administration of his duties hereunder.

14.3 A decision, act, consent or instruction of the Representative shall constitute a decision of all of the Sellers and shall be final, binding and conclusive upon each and every Seller, the Purchaser and the escrow agent under the Escrow Agreement, and the Purchaser and the escrow agent under the Escrow Agreement may rely upon any decision, act, consent or instruction of the Representative as being the decision, act, consent or instruction of each and every Seller. The Purchaser and the escrow agent under the Escrow Agreement are hereby relieved from any liability to any person for any acts done by them in accordance with such decision, act, consent or instruction of the Representative.

15 Final Provisions

15.1 The Parties agree that Commtouch shall be jointly liable for all obligations of the Purchaser under this agreement.

15.2 Where a German term has been inserted in this Agreement it alone (and not the English term to which it relates) shall be authoritative for the purpose of the interpretation of the relevant English term in this Agreement.

15.3 All changes of and amendments to this Agreement shall require the written form in order to be effective, unless being subject to notarization. This shall likewise apply to a waiver of the requirement-of-writing clause itself.

15.4 This Agreement shall be governed by the substantive laws of the Federal Republic of Germany.

15.5 Any notice or communication relating to this Agreement or its performance shall be sent in writing to the addresses of the contracting Parties shown above. These addresses shall remain applicable until changed by a contractual notice to all other Parties.

15.6 Should individual provisions of this Agreement be or become ineffective or should this Agreement prove to be incomplete, the effectiveness of the remaining provisions of this Agreement shall not be affected thereby. Rather, the Parties

shall in this case be under the obligation to replace the ineffective or missing provision by such effective provision as reflects best the economic purpose pursued by the ineffective or missing one.

The above Deed including all Annexes has been read aloud to the persons appearing in the presence of the notary, approved by them and signed by them and by the notary as follows:

Exhibit 4.8

SUMMARY OF TWO CREDIT LINES

During 2012, we made significant investments (from our cash reserves) in the above described acquisitions of eleven and Frisk. Due in part to these investments, at about the time of the filing of this Annual Report, a credit line had been secured from an Israeli bank, and we were in the process of closing on another credit line with a second Israeli bank. Together, both credit lines total a sum of up to $5,000,000. These credit lines are being put in place in order to ensure sufficient cash is available to fund the strategic growth investments of the Company.

In relation to these credit lines, the Company has agreed to grant security interests generally over all Company assets, and to refrain from encumbering its assets in favor of any other third parties. The Company has already drawn on one of the credit lines in the amount of $1.5 million.

Exhibit 8

LIST OF SUBSIDIARIES OF THE COMPANY

Commtouch Inc., a California corporation, and a wholly owned subsidiary of the Company, with offices in California, Virginia and Florida.

Commtouch Iceland hf, an Icelandic company, and a wholly owned subsidiary of the Company

eleven GmbH, a German company, held by the Company through a holding company arrangement. No entity outside of the Commtouch organization holds an ownership interest in eleven

Exhibit 12.1

CERTIFICATION PURSUANT TO EXCHANGE ACT RULE 13a-14(a) or 15d-14(a)

I, Shlomi Yanai, certify that:

1. I have reviewed this annual report on Form 20–F of Commtouch Software Ltd.;

2. Based on my knowledge, this annual 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 annual 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 Company's other certifying officer 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 Company 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 Company, 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 Company'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 Company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting; and

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

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 Company'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 Company's internal control over financial reporting.

Date: April 25, 2013

/s/Shlomi Yanai
Shlomi Yanai
Chief Executive Officer

Exhibit 12.2

CERTIFICATION PURSUANT TO EXCHANGE ACT RULE 13a-14(a) or 15d-14(a)

I, Brian Briggs, certify that:

1. I have reviewed this annual report on Form 20–F of Commtouch Software Ltd.;

2. Based on my knowledge, this annual 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 annual 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 Company's other certifying officer 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 Company 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 Company, 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 Company'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 Company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting; and

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

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 Company'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 Company's internal control over financial reporting.

Date: April 25, 2013

/s/Brian Briggs
Brian Briggs
Chief Financial Officer

Exhibit 13

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350

In connection with the Annual Report of Commtouch Software Ltd. (the "Company") on Form 20-F for the period ended December 31, 2012 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Shlomi Yanai and Brian Briggs, Chief Executive Officer and Chief Financial Officer of the Company, respectively, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to our knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange 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/Shlomi Yanai
Shlomi Yanai
Chief Executive Officer
April 25, 2013

/s/Brian Briggs
Brian Briggs
Chief Financial Officer
April 25, 2013

Exhibit 15

Consent of Independent Registered Public Accounting Firm

We consent to the reference to our firm under the caption "Experts" in the Registration Statement Form F-3 (No. 333-131272) and related Prospectus and on Form S-8 (File No. 333-94995, 333-141177, 333-65532, 333-151929, 333-162104, 333-174748, and 333-180453) pertaining to stock option plans of Commtouch Software Ltd., and to the incorporation by reference therein of our report dated April 25, 2013 with respect to the consolidated financial statements of Commtouch Software Ltd., included in this Annual Report (Form 20-F) for the year ended December 31, 2012.

/s/ Kost, Forer, Gabbay & Kasierer
A Member of Ernst & Young Global

Tel-Aviv, Israel
April 25, 2013