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COMMTOUCH SOFTWARE LTD

Form F-3

May 15, 2002

As filed with the Securities and Exchange Commission on May 15, 2002

Registration No. 333-

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM F-3
REGISTRATION STATEMENT
Under
THE SECURITIES ACT OF 1933

COMMTOUCH SOFTWARE LTD.
(Exact name of Registrant as specified in its charter)

Israel	Not Applicable
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

6 Hazoran Street
Poleg Industrial Park, P.O. Box 8511
Netanya 42504, Israel
011-972-9-863-6888
(Address and telephone number of Registrant's principal executive offices)

c/o Commtouch Inc.
Devyani Patel, Vice President, Finance
1300 Crittenden Lane, Suite # 102
Mountain View, California 94043
(650) 864-2000
(Name, address and telephone number of agent for service)

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Approximate date of commencement of proposed sale to the public: From time to time after the Registration Statement becomes effective.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. []

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, please check the following box. [X]

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If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. []

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. []

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. []

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Calculation of Registration Fee

Title of Each Class of Securities To Be Registered	Amount to be Registered	Proposed Maximum Aggregate Price Per Unit(1)	Proposed Maximum Aggregate Offering Price
ordinary shares, NIS 0.05 nominal value per share.....	7,095,886	\$0.16	\$1,135,341.76

(1) Estimated solely for the purpose of computing the amount of the registration fee pursuant to Rule 457(c) based on the average of the high and low prices of the Company's ordinary shares as reported on the Nasdaq National Market System on May 6, 2002.

(2) The Registrant initially filed a Registration Statement on Form F-1 (Registration No. 333-31836) on March 6, 2000 (the "Form F-1"), to register certain offers and sales of its ordinary shares as set forth in that Registration Statement. Subsequently, the Registrant withdrew the Form F-1 on April 12, 2000. The Registrant is filing this Registration Statement on Form F-3 to register the reoffer and resale of the securities indicated on this cover page. A registration fee of \$49,468.00 was paid in connection with the filing of the Form F-1. Pursuant to Rule 457(p), the aggregate total dollar amount of the filing fee associated with the unsold ordinary shares under the F-1 has previously been offset by the filing fees in the amounts of (a) \$119.80 for Registration Statement on Form S-8 No. 333-65532 filed on July 20, 2001; and (b) \$158.24 for Registration Statement on Form F-3 No. 333-68248 filed on August 24, 2001. The remaining balance of \$49,189.96 is being further offset by the filing fee due for this Registration Statement.

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THE INFORMATION IN THIS PROSPECTUS IS NOT COMPLETE AND MAY BE CHANGED. THE SELLING SECURITYHOLDERS MAY NOT SELL THESE SECURITIES UNTIL THE REGISTRATION STATEMENT FILED WITH THE SECURITIES AND EXCHANGE COMMISSION IS EFFECTIVE. THIS PROSPECTUS IS NOT AN OFFER TO SELL THESE SECURITIES AND IT IS NOT SOLICITING AN OFFER TO BUY THESE SECURITIES IN ANY STATE WHERE THE OFFER OR SALE IS NOT PERMITTED.

SUBJECT TO COMPLETION, DATED _____, 2002

PROSPECTUS

Commtouch Software Ltd.

7,095,886 Ordinary Shares

As we describe further below under "Offer Statistics and Expected Timetable and Plan of Distribution," the Selling Securityholders identified in this prospectus are selling up to 7,095,886 of our ordinary shares, some of which underlie warrants. The warrants themselves are not being offered by this prospectus. The Selling Securityholders acquired the ordinary shares from the Company in a private placement in April 2002 after approval by the Company's shareholders at a meeting held on April 8, 2002. The ordinary shares offered hereby have been registered pursuant to registration rights granted to the Selling Securityholders by the Company in connection with the private placement. These securities may be offered from time to time by the Selling Securityholders through public or private transactions, on or off the Nasdaq National Market, at prevailing market prices or at privately negotiated prices. The Selling Securityholders will receive all of the proceeds from this offering and will pay all underwriting discounts and selling commissions, if any, applicable to the sale of the securities. We will pay the expenses of registration of this offering.

The Company has agreed to indemnify the Selling Securityholders against certain liabilities, including liabilities under the Securities Act of 1933, as amended (the "Securities Act").

The ordinary shares are being offered by the Selling Securityholders subject to prior sale, subject to their right to reject offers in whole or in part and subject to certain other conditions.

The Selling Securityholders may be deemed to be "underwriters" within the meaning of the Securities Act and any profits realized by them may be deemed to be underwriting commissions. Any broker-dealers that participate in the distribution of ordinary shares also may be deemed to be "underwriters," as defined in the Securities Act, and any commissions or discounts paid to them, or any profits realized by them upon the resale of any securities purchased by them as principals, may be deemed to be underwriting commissions or discounts under the Securities Act. The sale of the ordinary shares is subject to the prospectus delivery requirements of the Securities Act.

Our ordinary shares are currently traded on the Nasdaq National Market under the symbol "CTCH." On May 10, 2002 the last reported sales price of an ordinary share on the Nasdaq National Market was \$0.16 per share.

This investment involves risk. See "Risk Factors" beginning on page ____.

Neither the Securities and Exchange Commission nor any state securities Commission has approved or disapproved of these securities or determined if this

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prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this Prospectus is , 2002

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SPECIAL NOTE REGARDING FORWARD-LOOKING INFORMATION

This document contains forward-looking statements that involve risks and uncertainties. These statements relate to our future plans, objectives, beliefs, expectations and intentions. In some cases, you can identify forward-looking statements by our use of words such as "expects," "anticipates," "believes," "intends," "plans," "seeks" and "estimates" and similar expressions. Our actual results, levels of activity, performance or achievements may differ materially from those expressed or implied by these forward-looking statements. Factors that could cause or contribute to these differences include those discussed in our Annual Report on Form 20-F, which is on file with the Securities and Exchange Commission.

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SUMMARY

We are a provider of email services and software for email and messaging solutions to service providers that target both residential and business subscriber users.

Our main target customers include companies that specialize in providing communications applications to enterprises, such as, ASPs, ISPs, telecoms, CLECs, wireless carriers, data centers, systems integrators, and IT consultants.

Email and messaging is complex and requires focus to implement, deliver and maintain. Today's solutions include the ability to address both front-end and back-end requirements, anytime-anywhere access, and features such as anti-virus protection, unified messaging, calendaring, group scheduling, file sharing, and collaboration. Technologies for the future are necessitating that email and messaging adapt and change with the new innovations. Our flexible technology and economies of scale enable us to provide email solutions in a cost-effective manner, intended to allow businesses to achieve desirable economic advantages. These technologies have been conceived, developed and refined over the course of

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the past 11 years, during which we have provided both services and software to a multitude of customers.

We offer software for email and messaging solutions to service providers, mainly small and medium size enterprises (SME). Service providers receive a license to install and use our software and technology in order to provide messaging and email services from their own data center facility. Our service provider solution enables service providers to easily manage the email and messaging features/services that they in turn provide to their end users.

We deliver a comprehensive software solution that -

- o Enables ISP business subscribers to enjoy advanced messaging applications.
- o Enables service providers to offer packages of email services. With Commtouch Classes of Service (CoS), service providers can create different packages of service to their diversified subscribers and market each package separately.
- o Enables service providers to simplify deployment and manageability of a highly-scalable messaging platform for residential and business subscribers, and to achieve high performance and maximized utilization at a competitive low cost (i.e. low hardware, bandwidth and administration costs).

Our solution provides:

- o Access to accounts from standard desktop email clients (e.g. Microsoft Outlook and Qualcomm Eudora), Web browsers and wireless devices, such as, WAP-enabled mobile phones.
- o Message notification on an advanced platform, to pagers, mobile phones, instant messengers and other email addresses.
- o Integrated, Web-based applications, including calendar, task manager, contact center, notes, short message service (SMS), and more.
- o Customization of the Web email client interface to extend an organization's brand.
- o Multiple language support for a multilingual user base.

Office Location

Our principal executive offices are located at 6 Hazoran Street, Poleg Industrial Park, Netanya 42504, Israel, where our telephone number is 011-972-9-863-6888, and 1300 Crittenden Lane, Suite # 102, Mountain View, California 94043, where our telephone number is (650) 864-2000. Our website address is www.commtouch.com.

Capitalization and Indebtedness

The following table sets forth the capitalization and indebtedness of Commtouch as of March 31, 2002, as adjusted for the private placement in April 2002:

(UNAUDITED)
(IN THOUSANDS)

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Long-term liabilities	\$ 269

Shareholders' equity:	
Ordinary shares, NIS 0.05 par value; 40,000,000 shares	
Authorized, 22,105,367 actual shares issued and	
outstanding	255
Additional paid-in capital	153,512
Deferred compensation	(690)
Notes receivable from shareholders	(752)
Accumulated deficit	(147,634)

Total shareholders' equity	\$ 4,691

Total capitalization	\$ 4,960
	=====

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 prospectus. 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 the market does not respond favorably to our new messaging solutions and related technologies, we will fail to generate revenues.

Our success will depend on the acceptance and use of our software messaging solutions by service providers to provide email services to their customers. We cannot estimate the size or growth rate of the potential market for our software offerings. If the market for email software fails to grow or grows more slowly than we currently anticipate, our business will suffer dramatically. Even if that market grows, our solutions may not achieve broad market acceptance. Since we have only recently released our new messaging platform for general distribution, we do not have experience to evaluate whether it will achieve broad market acceptance. Also, because a preponderance of our future revenue will be derived directly or indirectly from our software messaging solutions, if that market does not grow, our business will likely fail.

Our future revenues are unpredictable and our quarterly operating results may fluctuate which could adversely affect the value of your investment.

Because we have a limited history with our new email solutions and because of the emerging nature of the markets in which we compete, our revenue is unpredictable. Our current and future expense levels (although greatly reduced) are to a large extent fixed. We may be unable to adjust spending quickly to compensate for any revenue shortfall, and any significant revenue shortfall would have an immediate negative effect on our results of operations and share price.

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

- o The market acceptance of our new software messaging platform and related solutions
- o The size, timing and fulfillment of orders for our new software messaging solutions;
- o The success of our selling efforts to service providers;
- o The rate of adoption of new software messaging solutions by enterprise customers in the current economic environment;
- o The threat of de-listing by the NASDAQ;
- o The receipt or payment of irregular or nonrecurring revenues or expenses;
- o Our ability to successfully develop and market new solutions, as may be needed;
- o Pricing of our solutions; and
- o Effectiveness of our customer support.

Because of differing operational factors and the material changes to our business model, period-to-period comparisons of our operating results are not a good indication of our future performance. It is likely that our operating results in some quarters will be below market expectations. Because we are going to market with new solutions and have sold most of our hosted email service businesses, it is difficult to evaluate our business and prospects.

We commenced operations in 1991, but we are only beginning to try to sell our new software messaging solutions after having sold outsourced Web-based email services from 1998 through 2001, which itself was a change from our initial focus on the sale, maintenance and servicing of stand-alone email client software products for mainframe and personal computers. In late 2001 and early 2002, we sold our hosted exchange business and assigned most of our email service business to another company, to focus exclusively on developing and selling new software messaging technologies. This change required us to adjust our business processes and to restructure Commtouch. Therefore, we have no operating history as a provider of our new email technologies upon which you may be able to evaluate our business and prospects. It is too early to judge the success of this business.

We have many established competitors who are offering similar solutions

The market for messaging technologies is intensely competitive and we expect it to be increasingly competitive. Increased competition could result in pricing pressures, low operating margins and the realization of little or no market share, any of which could cause our business to suffer.

In the market for email and messaging software solutions, we compete directly with software solution providers, including Critical Path, OpenWave, iPlanet (Sun Microsystems), Mirapoint, Sendmail and Rockcliff, as well as with companies that develop and maintain in-house email solutions, such as Microsoft and IBM. Furthermore, certain small-scale email software providers offer low-cost basic solutions, but with limited scalability or value-added functionality. These and

other companies could potentially leverage their existing capabilities and relationships to enter the service provider email solutions industry.

Our market's level of competition is likely to increase as current competitors increase the sophistication of their offerings and as new participants enter the market. In the future, as we expand our offerings, we may encounter increased competition in the development and distribution of these solutions. Many of our current and potential competitors have longer operating histories, larger customer bases, greater brand recognition and greater financial, marketing and other resources than we do and may enter into strategic or commercial relationships on more favorable terms. In addition, new technologies and the expansion of existing technologies may increase competitive pressures on us. We may not be able to compete successfully against current and future competitors.

Our ability to increase our revenues will depend on our ability to successfully execute our sales and marketing plan.

The complexity of our software messaging solutions and the email software market require highly trained sales and marketing personnel to educate prospective customers regarding the use and benefits of our solutions. We have limited experience in selling software solutions to service provider customers. It will take time for our current and future employees to learn how to market our solutions. Additionally, we are unable to predict the success in selling newly introduced solutions in which we have no experience marketing and are relying on these solutions to produce a substantial portion of our revenues in the future. As a result of these factors, our sales and marketing organization may not be able to compete successfully against the bigger and more experienced sales and marketing organizations of our competitors.

We have a history of losses and may never achieve profitability.

We incurred net losses of approximately \$19.9 million in 1999, \$54.2 million in 2000 and \$61.0 in 2001. As of December 31, 2001, we had an accumulated deficit of approximately \$146.8 million. We have not achieved profitability in any period, and we might continue to incur net losses in the future. If we do not achieve profitability, our share price may decline further.

Possible Need For Additional Funds

The Company is very thinly capitalized. As such, we might become dependent upon raising additional funds to finance our business. Our cash balance at December 31, 2001 was \$2.2 million. If we are unable to raise additional funds, the Company could fail. There can be no assurance that we will be able to raise necessary funds or that we will be able to do so on terms acceptable to us. If needed, our inability to obtain adequate capital would limit our ability to continue our operations. Any such additional funding may result in significant dilution to existing stockholders.

Risk of Recession

Some of our former customers continue to operate in the dot-com market based on internet-centric business models and are experiencing a significant economic slowdown and an inability to raise additional capital.

These former customers were assigned to MailCentro, Inc. (a wholly owned subsidiary of CP Software Group, Inc.) and Telecomputing, Inc. in connection with the Company's agreements with these companies. According to these agreements entered into with MailCentro, Inc. and Telecomputing, Inc., the

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Company is expected to realize royalties on payments made by these former customers to MailCentro and Telecomputing (primarily in 2002). The ability of MailCentro and Telecomputing to collect outstanding receivables is significantly impacted by the liquidity issues of these customers, which may negatively impact our ability to recognize future revenue based on the afore-stated royalties. As a result, we may experience shortfalls in our future revenues.

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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 further 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, including Gideon Mantel, our Chief Executive Officer and Amir Lev, our President and Chief Technical Officer, could materially and adversely affect our business. The loss of our software developers may also adversely affect our messaging platform product, therefore 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 these key personnel. We cannot prevent them from leaving at any time. We do not maintain key-person life insurance policies on any of our employees.

Our recent head-count reduction from 210 employees to approximately 35 employees is significantly straining our operational resources. We have significantly curtailed sales and marketing resources and this may compromise our ability to enhance revenues.

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

At December 31, 2001 we had sales offices in Israel, United States and Japan. We intend to continue to seek ways to market our software messaging solutions in international markets by utilizing appropriate distributorship channels, i.e. by way of our joint strategic relationship with Unisys and other foreign representatives. We may not be able to compete effectively in international markets due to various risks inherent in conducting business internationally, such as:

- o differing technology standards;
- o inability of distribution channels to successfully market our software messaging solutions;
- o export restrictions, including export controls relating to encryption technologies;
- o difficulties in collecting accounts receivable and longer collection periods;
- o unexpected changes in regulatory requirements;
- o political and economic instability;
- o potentially adverse tax consequences; and
- o potentially reduced protection for intellectual property rights.

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

Terrorist attacks such as the attacks that occurred in New York and Washington, D.C. on September 11, 2001 and other attacks or acts of war may adversely affect the markets on which our ordinary shares trade, our financial condition and our results of operations.

On September 11, 2001, the United States was the target of terrorist attacks of unprecedented scope. These attacks have caused major instability in the U.S. and other financial markets. There could be further acts of terrorism in the United States or elsewhere that could have a similar impact. Leaders of the U.S. government have announced their intention to actively pursue and take military and other action against those behind the September 11, 2001 attacks and to initiate broader action against national and global terrorism. Armed hostilities or further acts of terrorism would cause further instability in financial markets and could directly impact our financial condition and our results of operations.

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Technology Risks

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

The internet messaging industry is characterized by rapid technological change, changes in end user requirements and preferences, and the emergence of new industry standards and practices that could render our solutions and proprietary technology obsolete. Our success depends, in part, on our ability to continually enhance our existing email and messaging solutions and to develop new solutions, functions and technology that address the increasingly sophisticated and varied needs of our prospective 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 customer or end user requirements or emerging industry standards. Also, we must be able to act more quickly than our competition.

Our software may be adversely affected by defects, which could cause our customers or end users to stop using our solutions.

Our solutions are based upon new and complex software. Complex software often contains defects, particularly when first introduced or when new versions are released. Although we conduct extensive testing, we may not discover software defects that affect our new or current solutions or enhancements until after they are delivered. Although we have not experienced any material software defects to date in our service offering, it is possible that, despite testing by us, defects may exist in the software we sell. These defects could cause service interruptions for our customers that could damage our reputation, create legal risks, cause us to lose revenue, delay market acceptance or divert our development resources, any of which could cause our business to suffer.

Investment Risks

We may need additional capital.

We have invested heavily in technology development. We expect to continue to

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spend financial and other resources on developing and introducing new offerings and maintaining our corporate organizations and strategic relationships. We also expect to invest resources in research and development projects to develop enhanced service provider messaging solutions.

Based on the cash balance at December 31, 2001, current projections of revenues, related expenses, the sale of the Wingra subsidiary and completion of the private investment round, the Company believes it has sufficient cash to continue operations for at least the next twelve months.

We are subject to a class action lawsuit which may have a material adverse effect on us.

Following our restatement of revenues for the first three quarters of 2000, several class action lawsuits were filed in the United States District Court for the Northern District of California against the Company and certain of our officers and a director, alleging violations of the antifraud provisions of the Securities Exchange Act of 1934 arising from the Company's financial statements. These lawsuits were consolidated into one action in late 2001. Thereafter, the Company filed a Motion to Dismiss, which has been granted, though the plaintiffs have been granted leave to amend the complaint, which they have done. The defendants have filed a Motion to Dismiss this amended complaint, and the matter is set for review by the court in mid-June 2002. While we are unable to predict the ultimate outcome of the consolidated claim, we believe that it is without merit and intend to continue to vigorously defend ourselves.

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If we cannot satisfy Nasdaq's maintenance requirements, it may delist our ordinary shares and we may not have an active public market for our ordinary shares, which would likely make our shares an illiquid investment.

Our ordinary shares are quoted on the Nasdaq National Market. To continue to be listed, our shares must have a minimum bid price of \$1.00 per share and we must maintain a minimum market value of our publicly held shares of \$5,000,000, among other requirements. Our shares have a minimum bid price of less than \$1.00 per share and the minimum market value is under \$5,000,000. Consequently, we do not satisfy the Nasdaq listing requirements and may not be able to do so in the future. Nasdaq has recently notified us that our stock may be delisted as of May 15, 2002. If this occurs, trading in the shares may be conducted in the over-the-counter market in the so-called "pink sheets" or, if available, the "OTC Bulletin Board Service." As a result, an investor would likely find it significantly more difficult to dispose of, or to obtain accurate quotations as to the value of, our shares.

Nasdaq also may delist our shares if it deems it necessary to protect investors and the public interest.

If our shares are delisted, they may become subject to the SEC's "penny stock" rules and be more difficult to sell.

SEC rules require brokers to provide information to purchasers of securities traded at less than \$5.00 and not traded on a national securities exchange or quoted on the Nasdaq Stock Market. If our shares become "penny stock" that is not exempt from these SEC rules, these disclosure requirements may have the effect of reducing trading activity in our shares and making it more difficult for investors to sell. The rules require a broker-dealer to deliver a standardized risk disclosure document prepared by the SEC that provides information about penny stocks and the nature and level of risks in the penny market. The broker must also give bid and offer quotations and broker and

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salesperson compensation information to the customer orally or in writing before or with the confirmation. The SEC rules also require a broker to make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser's written agreement to the transaction before a transaction in a penny stock.

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 own over five percent of our ordinary shares, beneficially own, in the aggregate, approximately 18.5% of our outstanding ordinary shares. If they vote together, these shareholders will be able to exercise significant influence over all matters requiring shareholder approval, including the election of directors and approval of significant corporate transactions. This concentration of ownership could also delay or prevent a change in control of Commtouch.

Jan Eddy, the President and Chief Executive Officer of Wingra Technologies, beneficially owns approximately 5% of our outstanding ordinary shares issued to her in connection with our acquisition of Wingra Technologies on November 24, 2000.

InfoSpace beneficially owns approximately 5% of our outstanding ordinary shares. InfoSpace merged with Go2Net in October 2000. In connection with this merger InfoSpace assumed Go2Net shares, warrants and rights. In 1999, in connection with entering into an email services agreement, we issued to InfoSpace a warrant to purchase 1,136,000 ordinary shares at an exercise price of \$12.80 per share. Concurrent with Commtouch Inc. entering into the email services agreement, we issued 896,057 ordinary shares to InfoSpace and 448,029 in ordinary shares to Vulcan Ventures in a private placement at \$14.88 per share. We believe that Vulcan Ventures divested itself of all of its shareholdings in the Company. The warrant is non-forfeitable, fully vested and immediately exercisable, and will expire in July 2004. Assuming exercise of the InfoSpace warrant on a net issuance basis, the warrant currently has no impact on beneficial ownership, as the warrant is currently underwater.

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Certain of the Selling Securityholders in this offering hold over 5% of our outstanding ordinary shares (See "Selling Securityholders" below).

These significant shareholders will be able to significantly influence and possibly exercise control over most matters requiring approval by our shareholders, including the election of directors and approval of significant corporate transactions. This concentration of ownership may also have the effect of delaying or preventing a change in control. InfoSpace will also have the right to name one director to our Board as long as it continues to hold at least 620,022 shares, including the shares issuable upon exercise of the InfoSpace warrant. It named Thomas Camp to the Board under this provision, who resigned on August 22, 2001 and was not replaced by Infospace. In addition, conflicts of interest may arise as a consequence of these significant shareholders control relationship with us, including:

- o 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;

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- o conflicts related to corporate opportunities that could be pursued by us, on the one hand, or by these shareholders, on the other hand; or
- o conflicts related to existing or new contractual relationships between us, on the one hand, and these shareholders, on the other hand.

Substantial sales of our ordinary shares could adversely affect our share price.

The sale, or availability for sale, of substantial quantities of our ordinary shares may have the effect of further depressing its market price. A large number of our ordinary shares which were previously subject to resale restrictions, are currently eligible for resale. In addition a significant number of shares will be eligible for resale at various dates in the future pursuant to this Registration Statement.

The shares issued to the Selling Securityholders will dilute existing shareholders.

Risk of failure to obtain registration rights for the private placement

According to the agreement with the Selling Securityholders, should the Company fail to meet certain deadlines for filing the Registration Statement and achieving the effectiveness thereof, the Company risks having imposed on it liquidated damages as defined in the agreement.

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 copyrights, service marks, trademarks, trade secrets and similar intellectual property as critical to our success, and rely on trademark and copyright law, trade secret protection and confidentiality or license agreements with our employees and customers to protect our proprietary rights. Third parties may infringe or misappropriate our copyrights, trademarks and similar proprietary rights. Although we have not filed any patent applications, we may seek to patent certain software or other technology in the future. Any such future patent applications may not be issued within the scope of the claims we seek, or at all. We cannot be certain that our software does not infringe issued patents that may relate to our software products. In addition, because patent applications in the United States are not publicly disclosed until the patent is issued, applications may have been filed which relate to our software products.

Despite our precautions, unauthorized third parties may copy certain portions of our technology or reverse engineer or obtain and use information that we regard as

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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. Our means of protecting our proprietary rights in the United States or abroad may not be adequate and competitors may independently develop similar technology.

Governmental regulation and legal uncertainties could impair the growth of the internet and decrease demand for our software messaging solutions or increase our cost of doing business.

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There are currently few laws and regulations directly applicable to the internet and commercial email services. However, a number of laws have been proposed involving the internet, including laws addressing user privacy, pricing, content, copyright, antitrust, distribution and characteristics and quality of products and services. Further, the growth and development of the market for email may prompt calls for more stringent consumer protection laws that may impose additional burdens on companies conducting business online. Moreover, the applicability to the internet of existing laws in various jurisdictions governing issues such as property ownership, sales and other taxes, libel and personal privacy is uncertain and may take years to resolve. The adoption of additional laws or regulations, or the application of existing laws or regulations to the internet, may impair the growth of the internet or commercial online services. This could decrease the demand for our software and increase our cost of doing business, or otherwise harm our business and operating results.

Risks Relating to Operations in Israel

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

We are incorporated under the laws of the State of Israel. Our principal research and development facilities are located in Israel. Although substantially all 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.

Israel's economy has been subject to numerous destabilizing factors, including a period of rampant inflation in the early to mid-1980's, low foreign exchange reserves, fluctuations in world commodity prices, military conflicts and civil unrest. In addition, Israel and some companies doing business with Israel have been the subject of an economic boycott by Arab countries since Israel's establishment. These restrictive laws and policies may have an adverse impact on our operating results, financial condition or expansion of our business.

Since the establishment of the State of Israel in 1948, a state of hostility has existed, varying in degree and intensity, between Israel and certain Arab countries. Since September 2000, a continuous armed conflict with the Palestinian Authority has been taking place. Although Israel has entered into various agreements with certain Arab countries and the Palestinian Authority, and various declarations have been signed in connection with efforts to resolve some of the economic and political problems in the Middle East, Israel continues to face hostile actions and threats from various elements in the region. We cannot predict whether or in what manner these problems will be resolved.

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. 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.

Because a substantial portion of our revenues are generated in U.S. dollars and a portion of our expenses are incurred in New Israeli Shekels, our results of operations may be adversely affected by inflation and currency fluctuations.

We generate a substantial portion of our revenues in U.S. dollars and incur a portion of our expenses, principally salaries and related personnel expenses in Israel, in New Israeli Shekels, commonly referred to as NIS. As a result, we are exposed to the risk that the rate of inflation in Israel will exceed the rate of devaluation of the NIS in relation to the dollar or that the timing of any devaluation may lag behind inflation in Israel. While in recent years the rate of devaluation of the NIS against the dollar has generally exceeded the rate of inflation, which is a reversal from prior years, we cannot be sure that this reversal will continue. If the dollar cost of our operations in Israel increases, our dollar-measured results of operations will be adversely affected. Our operations also could be adversely affected if we are unable to guard against currency fluctuations in the future. Accordingly, 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. These measures, however, may not adequately protect us from material adverse effects due to the impact of inflation in Israel.

The Government programs and benefits which we currently receive 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, or the OCS, for the financing of a significant portion of our research and development expenditures in Israel. In 2001 and 2002, we applied for additional grants and we may apply for additional grants in the future. In 1999 and 2000, we did not receive any grants from the OCS. In 2001 we received \$0.6 million and we expect the percentage of our research and development expenditures financed from OCS grants will continue to remain quite low. The OCS budget has been subject to reductions which may affect the availability of funds for these grants in the future. Therefore, we cannot be certain that we will continue to receive grants at the same rate, or at all. In addition, the terms of any future OCS grants may be less favorable than our past grants. In connection with research and development grants received from the OCS, we must pay royalties to the OCS on the revenue derived from the sale of products, technologies and services developed with grants from the OCS.

The terms of the OCS grants and the law pursuant to which the grants are made restrict our ability to manufacture products or transfer technologies developed using OCS grants outside of Israel. This restriction may limit our ability to enter into agreements for those products or technologies, without OCS approval. We cannot be certain that the approvals of the OCS will be obtained on terms that are acceptable to us, or at all. In connection with our grant applications, we have made representations and covenants to the OCS. The funding from the OCS is subject to the accuracy of these representations and covenants and to our compliance with the conditions and restrictions imposed by the OCS. If we fail to comply with any of these conditions or restrictions, we could be required to repay any grants previously received, together with interest and penalties, and would likely be ineligible to receive OCS grants in the future.

The projects for which we received grants from the OCS prior to 1998 ultimately failed and the relevant payments were made for the revenues generated from these projects. The Company will not be obligated to pay future royalties for such projects through 2001, since no future revenue is expected from these projects. Accordingly, the Company decided to write down the \$0.4 million accrual it recorded in past years and determined that as of December 31, 2001 there are no contingent liabilities for royalties from these projects. In March 2002, the

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Company submitted an application for project failure with regard to these projects. However, the ultimate liability is subject to the review of the Government of Israel. With regard to the grant received in 2001, a contingent liability of \$0.6 million exists.

The tax benefits we are currently entitled to from the Government of Israel may be reduced or terminated in the future.

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Pursuant to the Law for the Encouragement of Capital Investments, the Government of Israel through the Investment Center has granted "approved enterprise" status to a portion of our capital investment programs. The portion of our income derived from our approved enterprise program will be exempt from tax for a limited period of two years commencing in the first year in which we have taxable income, and will be subject to a reduced tax for an additional period of five to eight years dependent on the percentage of foreign shareholders. The benefits available to an approved enterprise are conditioned upon the fulfillment of conditions regarding a required amount of investments in fixed assets and a portion of these investments being made with net proceeds of equity capital raised by us as stipulated in applicable law and in the specific certificates of approval. If we fail to comply with these conditions, in whole or in part, we may be required to pay additional taxes for the period in which we benefited from the tax exemption or reduced tax rates and would likely be denied these benefits in the future. From time to time, the Government of Israel has discussed reducing or eliminating the benefits available under the approved enterprise program. It is possible that these tax benefits may not be continued in the future at their current levels or at all.

Israeli courts might not enforce judgments rendered outside of Israel and it might therefore be difficult for an investor to recover any judgment against any of our officers or directors resident in Israel.

We are organized under the laws of Israel, and we maintain significant operations in Israel. Certain of our officers and directors named in this prospectus reside outside of the United States. Therefore, you might not be able to enforce any judgment obtained in the U.S. against us or any of such persons. You might not be able to bring civil actions under U.S. securities laws if you file a lawsuit in Israel. However, we have been advised by our Israeli counsel that, subject to certain limitations, Israeli courts may enforce a final judgment of a U.S. court for liquidated amounts in civil matters after a hearing in Israel. We have appointed Commtouch Software Inc., our U.S. subsidiary, as our agent to receive service of process in any action against us arising from this prospectus. We have not given our consent for our agent to accept service of process in connection with any other claim and it may therefore be difficult for an investor to effect service of process against us or any of our non-U.S. officers, directors and experts relating to any other claims. If a foreign judgment is enforced by an Israeli court, it may be payable in Israeli currency.

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, votes required to approve 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, Israel tax considerations may make potential transactions unappealing to us or to some of our shareholders.

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Proposed tax reform in Israel may reduce our tax benefits, which might adversely affect our profitability.

On May 4, 2000, a committee chaired by the former Director General of the Israeli Ministry of Finance issued a report recommending a sweeping reform in the Israeli system of taxation. The proposed reform would significantly alter the taxation of individuals, and would also affect corporate taxation. In particular, the proposed reform would reduce, but not eliminate, the tax benefits available to approved enterprises such as ours. The Israeli cabinet approved the recommendations in principle, but implementation of the reform requires legislation by Israel's Knesset. In the interim there have been significant political and economic changes. On February 26, 2002 the Minister of Finance appointed a new committee to recommend tax reforms, and this committee is expected to submit a report within 90 days. The Company cannot be certain whether the proposed reform will be adopted, when it will be adopted or what form any reform will ultimately take.

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You should rely only on the information contained in this prospectus. We have not authorized any other person to provide you with different information. This prospectus is not an offer to sell, nor is it seeking an offer to buy, these securities in any jurisdiction where the offer or sale is not permitted. The information in this prospectus is complete and accurate as of the date on the front cover, but the information may have changed since that date.

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THE OFFER AND LISTING

The Offering

Ordinary shares offered	7,095,886 shares
Ordinary shares outstanding after the offering prior to the offering on April 16, 2002 of 22,105,367]	24,766,322 shares [based on ordinary shares outstanding
Use of proceeds	We will not receive any of the proceeds from the sale of the shares by the Selling Securityholders in this offering.
NASDAQ National Market Symbol	CTCH

Shares will be offered on a registered basis and not as bearer shares.

Except as otherwise specified, all information in this prospectus is based on the number of shares outstanding as of December 31, 2001, and:

- o assumes the issuance of 298,538 ordinary shares issuable upon exercise of options granted to executive officers and directors within 60 days of December 31, 2001 at a weighted average exercise

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price of \$0.31 per share; and

- o with respect to financial information, is reported in U.S. dollars;

and does not include:

- o 2,915,689 ordinary shares issuable to employees and consultants upon exercise of outstanding options under our stock option plans and stock option agreements as of December 31, 2001 at a weighted average exercise price of \$0.46; and
- o 2,303,885 ordinary shares available for future grant or issuance under our stock option and stock purchase plans as of December 31, 2001.

Market Information

The Company's Ordinary Shares have traded publicly on The Nasdaq Stock Market under the symbol "CTCH" since July 13, 1999.

The following