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DELTATHREE INC (DDDC)

Form 10-Q

Filed: November 12, 2009 (Period: September 30, 2009)

Quarterly report which provides a continuing view of a company's financial position

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

FORM 10-Q

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

For the quarterly period ended September 30, 2009

or

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

For the transition period from _____ to _____

Commission File Number: 000-28063

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

Delaware

(State or other jurisdiction of incorporation or organization)

13-4006766

(I.R.S. Employer Identification Number)

224 West 35th Street, New York, N.Y.

(Address of principal executive offices)

10001-2533

(Zip Code)

(212) 500-4850

(Registrant's telephone number, including area code)

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 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, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Non-accelerated filer

Accelerated filer

Smaller reporting company

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

As of November 9, 2009, the registrant had outstanding 71,932,405 shares of common stock, par value \$0.001 per share.

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements

DELTATHREE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)
(\$ in thousands)

	As of September 30, 2009	As of December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 2,367	\$ 1,788
Restricted cash and short-term investments	317	317
Accounts receivable, net	443	760
Prepaid expenses and other current assets	403	398
Inventory	28	33
Total current assets	3,558	3,296
Property and equipment, net	771	1,441
Deposits	68	117
Total assets	\$ 4,397	\$ 4,854
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of capital leases	\$ 161	\$ 148
Accounts payable and accrued expenses	2,005	1,485
Deferred revenues	858	771
Other current liabilities	1,661	1,615
Total current liabilities	4,685	4,019
Long-term liabilities:		
Capital leases, net of current portion	25	147
Severance pay obligations	99	140
Total long-term liabilities	124	287
Total liabilities	4,809	4,306
Stockholders' equity:		
Common stock, par value \$0.001 per share - authorized: 200,000,000 shares; issued and outstanding: 32,870,105 at December 31, 2008, and 71,962,405 at September 30, 2009.	72	33
Additional paid-in capital	174,207	173,137
Accumulated deficit	(174,691)	(172,622)
Total stockholders' equity	(412)	548
Total liabilities and stockholders' equity	\$ 4,397	\$ 4,854

See notes to unaudited condensed consolidated financial statements.

DELTATHREE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)
(\$ in thousands, except share and per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Revenues	\$ 4,814	\$ 4,792	\$ 15,319	\$ 15,580
Costs and operating expenses:				
Cost of revenues	4,034	3,414	12,798	11,269
Research and development expenses	94	607	334	2,857
Selling and marketing expenses	227	638	914	3,055
General and administrative expenses	650	692	2,627	1,897
Restructuring costs	-	-	-	957
Write-down of Go2call intangible asset	-	3,091	-	3,566
Deferred revenue restatement	-	-	-	596
Depreciation and amortization	197	478	723	1,494
Total costs and operating expenses	<u>5,202</u>	<u>8,920</u>	<u>17,396</u>	<u>25,691</u>
Loss from operations	(388)	(4,128)	(2,077)	(10,111)
Capital gain	72	-	86	-
Other non-operating income	-	7	15	18
Interest (expense), net	(32)	93	(64)	23
Net loss before taxes	(348)	(4,028)	(2,040)	(10,070)
Income taxes	19	12	29	27
Net loss	<u>\$ (367)</u>	<u>\$ (4,040)</u>	<u>\$ (2,069)</u>	<u>\$ (10,097)</u>
Basic net loss per share	<u>\$ (0.01)</u>	<u>\$ (0.12)</u>	<u>\$ (0.03)</u>	<u>\$ (0.31)</u>
Basic weighted average number of shares outstanding	<u>71,962,405</u>	<u>32,870,105</u>	<u>71,962,405</u>	<u>32,870,105</u>

See notes to unaudited condensed consolidated financial statements.

DELTATHREE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(\$ in thousands)

	Nine Months Ended September 30,	
	2009	2008
Cash flows from operating activities:		
Loss for the period	\$ (2,069)	\$ (10,097)
Adjustments to reconcile loss for the period to net cash used in operating activities:		
Depreciation of property and equipment	723	1,156
Amortization of intangible assets	-	338
Write-off of fixed asset	20	-
Stock-based compensation	35	285
Capital gain	(86)	(2)
Provision for losses on accounts receivable	186	121
Change in liability for severance pay, net	(41)	(162)
Exchange rates differences on deposits, net	(1)	(5)
Deferred revenue adjustments	-	596
Write-down of Go2call intangible asset	-	3,566
Changes in assets and liabilities:		
Decrease in accounts receivable	131	150
(Increase) decrease in prepaid expenses and other current assets	(53)	33
Decrease in inventory	5	112
Increase (decrease) in accounts payable and accrued expenses	520	(848)
Increase (decrease) in deferred revenues	87	(70)
Increase (decrease) in other current liabilities	46	(329)
Increase in other long-term liabilities	-	181
	1,604	5,122
Net cash used in operating activities	(497)	(4,975)
Cash flows from investing activities:		
Change in long-term deposits	50	50
Purchase of property and equipment	(142)	(327)
Proceeds from disposal of property and equipment	156	21
Decrease in short-term investments	-	5,501
Net cash provided by investing activities	64	5,245
Cash flows used in financing activities:		
Release of restricted cash	47	-
Proceeds from exercise of employee options	4	-
Proceeds from issuance of shares, net	1,070	-
Payment of capital leases	(109)	(80)
Net cash provided by (used in) financing activities	1,012	(80)
Increase in cash and cash equivalents	579	190
Cash and cash equivalents at beginning of period	1,788	1,649
Cash and cash equivalents at end of period	\$ 2,367	\$ 1,839

**Nine Months Ended
September 30,**

2009 2008

Supplemental schedule of cash flow information:

Cash paid for:

Taxes	\$ 25	\$ 14
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Supplemental schedule of investing and financing activities:

Acquisition of capital leases	\$ -	\$ 198
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Cash received from:

Proceeds from issuance of shares	1,170	-
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Direct costs paid for services due to issuance of shares	100	\$ -
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Total proceeds	<u>1,070</u>	<u>-</u>
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See notes to unaudited condensed consolidated financial statements.

DELTAHREE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Basis of Presentation

Financial Statement Preparation

The unaudited condensed consolidated financial statements of deltatree, Inc. and its subsidiaries (collectively referred to in this Quarterly Report on Form 10-Q as the “Company”, “we”, “us”, or “our”), of which these notes are a part, have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the instructions of Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of our management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation of the financial information as of and for the periods presented have been included.

The results for the interim periods presented are not necessarily indicative of the results that may be expected for any future period. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes for the year ended December 31, 2008, included in our Annual Report on Form 10-K filed with the SEC on April 15, 2009, our Quarterly Report on Form 10-Q for the quarter ended March 31, 2009, filed with the SEC on May 15, 2009, our Quarterly Report on Form 10-Q for the quarter ended June 30, 2009, filed with the SEC on August 14, 2009, and all of our other periodic filings, including Current Reports on Form 8-K, filed with the SEC after the end of our 2008 fiscal year and through the date of this Report.

In June 2009, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 168, “The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles” (SFAS No. 168) [ASC 105-10]. SFAS No. 168 replaces SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles” and establishes the FASB Accounting Standards Codification (the “Codification”) as the source of authoritative accounting principles recognized by the FASB to be applied by non-governmental entities in the preparation of financial statements in conformity with GAAP. Rules and interpretive releases of the SEC issued under the authority of federal securities laws will continue to be sources of authoritative GAAP for SEC registrants. The Codification has become the exclusive authoritative reference effective September 30, 2009. This Form 10-Q includes the new Codification numbering system along with the former references.

Going Concern

The Company has sustained significant operating losses in recent periods, which has resulted in a significant reduction in its cash reserves. As of September 30, 2009, the Company had negative working capital equal to approximately \$1,127,000 as well as negative stockholders’ equity equal to approximately \$412,000. Management believes that the Company will continue to experience losses and increased negative working capital and negative stockholders’ equity in the near future and may not be able to return to positive cash flow before it requires additional cash. There can be no assurance that the Company will be able to raise such additional capital on favorable terms or at all. If additional funds are raised through the issuance of equity securities, the Company’s existing stockholders might experience significant further dilution. There can be no assurance that the Company’s financial condition will improve in the foreseeable future. As a result of the foregoing factors, there is substantial doubt about the Company’s ability to continue as a going concern.

Use of Estimates

Our consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States, which require management to make estimates and assumptions that affect the amounts reported and disclosed in the consolidated financial statements and the accompanying notes. Actual results could differ materially from these estimates.

Earnings per Common Share

Basic earnings per common share is computed by dividing net income by the weighted-average number of shares of common stock outstanding during the reporting period. Diluted earnings per common share is computed by dividing net income by the combination of dilutive common share equivalents, comprised of shares issuable under the Company's stock option and stock incentive compensation plans, and the weighted-average number of shares of common stock outstanding during the reporting period. Dilutive common share equivalents include the dilutive effect of in-the-money shares, which is calculated based on the average share price for each period using the treasury stock method. Under the treasury stock method, the exercise price of a share, the amount of compensation cost, if any, for future service that the Company has not yet recognized, and the amount of estimated tax benefits that would be recorded in additional paid-in capital, if any, when the share is exercised are assumed to be used to repurchase shares in the current period.

2. Stock-Based Compensation

A. Options

Share-based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period in accordance with the provisions of FASB Statement No. 123R, "Accounting for Stock-Based Compensation" (FAS 123R) [ASC 718-10]. The Company adopted the provisions of FAS 123R [ASC 718-10] on January 1, 2006, the first day of the Company's fiscal year in 2006, using a modified prospective application. Under the modified prospective method, prior periods' grant date fair values are not revised. The valuation provisions of FAS 123R [ASC 718-10] apply to new awards and to awards that are outstanding on the effective date and subsequently modified or cancelled. Estimated compensation expense for awards outstanding at the effective date will be recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under FAS 123R [ASC 718-10].

The Company has no awards with market or performance conditions.

The Company used the implied volatility market-traded options in the Company's stock for the expected volatility assumption input in the Black-Scholes model, consistent with the guidance in FAS 123R [ASC 718-10].

The risk-free interest rate assumption is based upon observed interest rates appropriate for the terms of the Company's employee stock options. The Company does not target a specific dividend yield for its dividends payments but is required to assume a dividend yield as an input to the Black-Scholes model. The dividend yield assumption is based on the Company's history and expectation of future dividends payout and may be subject to substantial change in the future. The expected life of employee stock options represent the period the stock options are expected to remain outstanding. The Black-Scholes model assumes that an employee's exercise behavior is a function of the option's remaining contractual life and the extent to which the option is in-the-money (i.e., the average market price of the underlying stock during the period is above the strike price of the stock option).

Options to purchase an aggregate of 3,740,000 shares of the Company's common stock were granted during the three months ended September 30, 2009.

B. Restricted shares and restricted units to purchase shares of the Company's common stock

The Company grants restricted shares to retain, reward and motivate selected employees and directors whom we believe are critical to the future success of the Company. We record compensation expense associated with non-vested restricted shares that have been granted in accordance with FAS 123R [ASC 718-10]. In accordance with FAS 123R [ASC 718-10], we calculate compensation expense on the date of grant (number of shares granted multiplied by the fair value of our common stock on the date of grant) and recognize this expense, adjusted for forfeitures, ratably over the applicable vesting period.

There were no restricted shares granted during the three months ended September 30, 2009.

3. Commitments and Contingencies

Lease Commitments

Delta Three Israel Ltd, a wholly-owned subsidiary of the Company (the "Subsidiary"), leases a 1,290 square meter office that houses the Company's research and development facilities in Jerusalem, Israel. On October 20, 2009, the Subsidiary and the landlord executed an amendment to the Lease Agreement pursuant to which, retroactive to July 1, 2009, the number of square meters comprising the office space under the lease was reduced by 556 square meters and the term of the lease was extended to June 30, 2012, with an option for the Subsidiary to extend the term for an additional 36 months thereafter. Rent expense, net for the Subsidiary was \$42,000 for the three months ended September 30, 2009.

Legal Proceedings

On December 5, 2008, a complaint for patent infringement was filed in the United States District Court for the Eastern District of Texas (Tyler Division) by Centre One naming the Company, Verizon Communications Inc., Vonage Holdings Corp. and Vonage America Inc. as defendants. The complaint alleges, *inter alia*, that the Company and Verizon are offering for sale “a VoIP service, including, but not limited to, a service under the name Verizon VoiceWing” that infringes United States Patent No. 7,068,668, or Patent '668, entitled “Method and Apparatus for Interfacing a Public Switched Telephone Network and an Internet Protocol Network for Multi-Media Communication.”

On March 6, 2009, the Company filed an Answer and Counterclaim, in which it denied that it has infringed Patent '668 and sought declaratory judgments that: it has not infringed Patent '668; any alleged infringement would not be actionable due to one or more of the Company's affirmative defenses; and Patent '668 is invalid and unenforceable due to inequitable conduct and a failure to meet the requirements of patentability.

On April 7, 2009, the court held a status conference and assigned May 6, 2010, and December 6, 2010, as the dates for the pretrial hearing to interpret the construction of Centre One's claims and the commencement of the trial, respectively.

On June 9, 2009, Centre One served a Disclosure of Asserted Claims and Infringement Contentions, in which it accused certain of the Company's VoIP services, in addition to Verizon VoiceWing, of infringing Patent '668. Centre One identified the Company's Hosted Consumer VoIP Solutions, Consumer Group Global Internet Phone Service, and Reseller Programs as allegedly infringing.

On June 22, 2009, the United States Patent and Trademark Office (the “PTO”) granted a request by Verizon Long Distance LLC to reexamine Patent '668, and issued a non-final office action rejecting all but two of the 37 claims of Patent '668 as not patentable. On July 8, 9, and 10, 2009, the Company and the other defendants moved to stay the litigation in the Eastern District of Texas pending the PTO's reexamination of Patent '668. Centre One opposed the stay motions on July 10, 2009. The court has not yet ruled on the stay motions.

On July 14, 2009, Verizon Long Distance, and on August 13, 2009, the Company and Vonage, filed Invalidity Contentions seeking to invalidate under 35 U.S.C. §102 and/or §103 all of the claims of Patent '668 asserted over prior patents and publications of third parties not disclosed to the PTO at the time that Patent '668 was granted.

On August 24, 2009, Centre One amended at the PTO 12 of the 21 claims it had asserted in the litigation. On September 18, 2009, Centre One moved to amend its Infringement Contentions to withdraw the claims it had amended at the PTO and to assert two additional claims of infringement. The Company and the other defendants agreed to the withdrawn claims but opposed Centre One's attempt to assert new claims. The court has not yet ruled on the motion.

The Company's initial examination of the allegations set forth in the Complaint leads the Company to firmly believe that it does not infringe any valid claim of Patent '668. The Company is continuing its examination into the allegations set forth in the complaint and the validity of Patent '668, and cannot predict with any degree of certainty the results of its examination and/or the outcome of the suit or determine the extent of any potential liability or damages.

In addition, from time to time the Company is a party to legal proceedings, much of which is ordinary routine litigation incidental to the business, and is regularly required to expend time and resources in connection with such proceedings. Accordingly, the Company, in consultation with its legal advisors, accrues amounts that management believes it is probable the Company will be required to expend in connection with all legal proceedings to which it is a party.

Regulatory Taxes, Fees and Surcharges

The Company has completed a study of FCC-related fees that are due and has accrued approximately \$200,000 of estimated fees. The Company has recently filed with the FCC the required reports disclosing the amounts it believes are due. The Company expects to pay such fees in the near future upon receipt of invoices corresponding to such reports and, if necessary, to adjust the accrual.

In addition, some state and local regulatory authorities believe they retain jurisdiction to regulate the provision of, and impose taxes, fees and surcharges on, intrastate Internet and VoIP telephony services, and have attempted to impose such taxes, fees and surcharges, such as a fee for providing E-911 service. Rulings by the state commissions on the regulatory considerations affecting Internet and IP telephony services could affect the Company's operations and revenues, and the Company cannot predict whether state commissions will be permitted to regulate the services the Company offers in the future.

The Company is in the process of examining the applicability of such state and other local taxes and other fees. It has completed a study of state and local taxes and other fees and has accrued approximately \$500,000 of estimated taxes and other fees. It has also determined that it needs to collect and remit sales and excise taxes in certain states and local jurisdictions and will begin collecting and remitting such sales and excise taxes in the immediate future. To the extent the Company increases the cost of services to its customers to recoup some of the costs of compliance, this will have the effect of decreasing any price advantage the Company may have over traditional telecommunications companies.

In addition, it is possible that the Company will be required to collect and remit taxes, fees and surcharges in other states and local jurisdictions where it has not done so, and which such authorities may take the position that the Company should have collected. If so, such regulatory authorities may seek to collect those past taxes, fees and surcharges from the Company and impose fines, penalties or interest charges on the Company. Our payment of these past taxes, fees and surcharges, as well as penalties and interest charges, could have a material adverse effect on the business, results of operations and financial condition of the Company.

4. Subsequent Events

On October 9, 2009, the Company and Ojo Service, LLC ("OJO Service"), a wholly-owned subsidiary of WorldGate Communications, Inc. ("WorldGate"), entered into a Master Service Agreement (the "Agreement") pursuant to which the Company will provide OJO Service wholesale voice-over-IP telephony and video services in the United States. Pursuant to the terms of the Agreement, OJO Service will pay the Company an activation fee and monthly subscriber fee for each customer of OJO Service that subscribes to the services provided by the Company to OJO Service. If OJO Service does not incur charges payable to the Company of at least \$300,000 during the six month period following the date that the first subscriber of OJO Service is provided service, OJO Service will be obligated to pay the Company an amount equal to 33% multiplied by the difference between \$300,000 and the actual amount of such charges during such six month period. The Company will provide such services for a period of five years from the date OJO Service begins offering the services provided under the Agreement to its subscribers. The term will renew automatically for successive terms of one year each unless either party provides the other party written notice of termination at least 180 days prior to the expiration of the then-current term. The Agreement can be terminated by either party for cause or upon 180 days notice for convenience. As further discussed below under "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations – Overview", the Company is majority-owned by D4 Holdings, LLC ("D4 Holdings"). WorldGate is majority-owned by WGI Investor LLC ("WGI Investor"). D4 Holdings and WGI Investor have common majority ownership and a common manager.

On November 3, 2009, the Company was informed that the operations of its largest customer had been suspended. In 2008, this customer accounted for approximately 16.5% of the Company's annual gross revenues, and in the third quarter of 2009 this customer accounted for approximately 29% of the Company's gross revenues. At this time the Company does not know if or when such customer will resume its operations or if, following any such resumption of operations, the Company and such customer will resume their commercial relationship. The loss of revenue attributable to this customer could have a material adverse effect on the Company's financial condition and results of operations.

A dispute has recently arisen with one of our vendors regarding our potential liability for the unauthorized use of our network by an outside third party. We believe that the total amount of such potential liability may be up to approximately \$600,000. Although we believe that, for various reasons, we may not be required to assume such liability, in the event that we are required to pay all or part of such amount this could have a material adverse effect on our financial condition and results of operations.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Management's Discussion and Analysis of Financial Condition and Results of Operations, or MD&A, should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and the Notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2008.

Forward-Looking Statements

This MD&A contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are based on current expectations, estimates, forecasts and projections about us, our future performance, the industries in which we operate our beliefs and our management's assumptions. In addition, other written or oral statements that constitute forward-looking statements may be made by us or on our behalf. Words such as "may," "expect," "anticipate," "forecast," "intend," "plan," "believe," "seek," "estimate," variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to assess. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. These risks and uncertainties include, but are not limited to, the following:

- our ability to obtain additional capital in the near term to finance operations;
- our ability to reduce our costs and expenses and expand our revenues;
- our ability to retain key personnel and employees needed to support our services and ongoing operations;
- our failure to retain key customers;
- decreasing rates of all related telecommunications services;
- the public's acceptance of Voice over Internet Protocol, or VoIP, telephony, and the level and rate of customer acceptance of our new products and services;
- the competitive environment of Internet telephony and our ability to compete effectively;
- fluctuations in our quarterly financial results;
- our ability to maintain and operate our computer and communications systems without interruptions or security breaches;
- our ability to operate in international markets;
- our ability to provide quality and reliable service, which is in part dependent upon the proper functioning of equipment owned and operated by third parties;
- the uncertainty of future governmental regulation;
- the need for ongoing product and service development in an environment of rapid technological change; and
- other risks referenced from time to time in our filings with the SEC.

For a more complete list and description of such risks and uncertainties, as well as other risks, please refer to the section entitled "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2008. Except as required under the federal securities laws and the rules and regulations promulgated thereunder, we do not have any intention or obligation to update publicly any forward-looking statements or risk factors after the distribution of this MD&A, whether as a result of new information, future events, changes in assumptions or otherwise.

Overview

We are a well-known provider of integrated Voice over Internet Protocol, or VoIP, telephony services, products, hosted solutions and infrastructure. We were founded in 1996 to capitalize on the growth of the Internet as a communications tool by commercially offering Internet Protocol, or IP, telephony services, or VoIP telephony. VoIP telephony is the real-time transmission of voice communications in the form of digitized "packets" of information over the Internet or a private network, similar to the way in which e-mail and other data is transmitted. While we began as primarily a low-cost alternative source of wholesale minutes for carriers around the world, we have evolved into a well-known provider of next generation communication services.

Today we support tens of thousands of active users around the globe through our two primary distribution channels: our service provider and reseller channel, and our direct-to-consumer channel. We offer a broad suite of private label VoIP products and services as well as a back-office platform for service providers, resellers and corporate customers, such as VoIP operators and various corporate enterprises. Based on our customizable VoIP solutions, these customers can offer private label telecommunications to their own customer bases under their own brand name, a "white-label" brand (in which no brand name is indicated and different customers can offer the same product), or the deltathree brand. At the same time, our direct-to-consumer channel includes our iConnectHere offering (which provides VoIP products and services directly to consumers and small businesses online using the same primary platform) and our joip offering (which serves as the exclusive VoIP service provider embedded in the Globalrange cordless phones of Panasonic Communications).

Following a comprehensive review of the company's strategy in the second quarter of 2009, we decided to focus our near-term strategy and market initiatives on growing our service provider business while still supporting our core VoIP reseller and direct-to-consumer business segments. While our revenues for the third quarter of 2009 remained substantially similar to our revenues for the second quarter of 2009, our net loss decreased from approximately \$1,261,000 to approximately \$367,000. As of September 30, 2009, we had negative working capital equal to approximately \$1,127,000 and negative stockholders' equity equal to approximately \$412,000.

On February 12, 2009, we consummated a transaction with D4 Holdings, LLC, or D4 Holdings, pursuant to which, among other things, D4 Holdings acquired (i) 39,000,000 shares of our common stock, representing approximately 54.3% of the total number of issued and outstanding shares of our common stock following the transaction and (ii) a warrant, exercisable for ten years, to purchase up to an additional 30,000,000 shares of our common stock at an exercise price of \$0.04 per share. D4 Holdings is a private investment fund whose ownership includes owners of ACN, Inc., or ACN, a direct seller of telecommunications services. As a result of the investment in our company by D4 Holdings, we expect to seek opportunities to provide services to ACN and enter into other commercial transactions that give us access to ACN's international marketing and distribution capabilities. On July 29, 2009, we entered into an agreement with ACN Pacific Pty Ltd., or ACN Pacific, a wholly-owned subsidiary of ACN, pursuant to which we provide digital phone and video VoIP telecommunications services to ACN Pacific. ACN Pacific provides such services in combination with the products and services it makes available to be resold by its independent sales representatives in Australia. Under the agreement, ACN Pacific is required to pay us a one-time set-up fee of \$260,000 and will pay us a monthly subscriber-based fee going forward. We will provide services under the agreement for a period of two years from the launch of the services in mid-August 2009. The agreement can be terminated by either party for cause or upon 120 days notice, and by ACN Pacific upon 30 days notice if the parties cease to remain affiliated entities. In addition, on October 9, 2009, we entered into an agreement with Ojo Service, LLC, a wholly-owned subsidiary of WorldGate Communications, Inc., pursuant to which we will provide OJO Service wholesale voice-over-IP telephony and video services in the United States. Pursuant to the terms of the agreement, OJO Service will pay us an activation fee and monthly subscriber fee for each customer of OJO Service that subscribes to the services provided by us to OJO Service. If OJO Service does not incur charges payable to us of at least \$300,000 during the six month period following the date that the first subscriber of OJO Service is provided service, OJO Service will be obligated to pay us an amount equal to 33% multiplied by the difference between \$300,000 and the actual amount of such charges during such six month period. We will provide such services for a period of five years from the date OJO Service begins offering the services provided under the agreement to its subscribers. The term will renew automatically for successive terms of one year each unless either party provides the other party written notice of termination at least 180 days prior to the expiration of the then-current term. The agreement can be terminated by either party for cause or upon 180 days notice for convenience. Worldgate is majority-owned by WGI Investor LLC, which has common majority ownership and a common manager with D4 Holdings, the holder of a majority of our outstanding securities. Each of Robert Stevanovski, Anthony Cassara, David Stevanovski and Gregory Provenzano serves on our board of directors and the board of directors of WorldGate, and each has an indirect ownership interest in D4 Holdings and WGI Investor.

Results of Operations - Three Months Ended September 30, 2009, Compared to Three Months Ended September 30, 2008

Revenues

Revenues for the three months ended September 30, 2009, totaled \$4.8 million, the same as for the three months ended September 30, 2008. Revenues from our reseller and service provider divisions increased by approximately \$0.2 million, or 6%, to approximately \$4.3 million for the three months ended September 30, 2009, from approximately \$4.1 million for the three months ended September 30, 2008. This occurred primarily as a result of an increase in revenues generated by our largest reseller from zero in the third quarter of 2008 to approximately \$1.4 million in the third quarter of 2009 offset by a significant decrease in revenues generated by our smaller resellers during that period. In addition, revenues from our second largest reseller increased slightly from approximately \$0.9 million in the third quarter of 2008 to approximately \$1.0 million in the third quarter of 2009.

Within the reseller business itself, we made a decision in the first quarter of 2009 to focus on servicing fewer, larger resellers rather than more, smaller resellers. Consequently, our two largest resellers accounted for approximately \$2.4 million, or approximately 63%, of the revenue generated from our reseller division in the third quarter of 2009. This represented approximately 50% of our total revenue for the third quarter of 2009. By comparison, in the third quarter of 2008 our two largest resellers accounted for approximately \$1.3 million, or approximately 40%, of the revenue generated from our reseller division, which equaled approximately 27% of our total revenue for the third quarter of 2008.

Revenues generated by our service provider division decreased by approximately \$0.4 million, or 44%, to \$0.5 million for the three months ended September 30, 2009, from \$0.9 million for the three months ended September 30, 2008, primarily due to the termination of our agreements with two customers. This included the termination of our agreement with our largest service provider client, which accounted for revenue of approximately \$0.5 million in the third quarter of 2008 (representing approximately 10% of our gross revenues for that quarter). As a result of the termination of this agreement we did not receive any revenues for this client in the three months ended September 30, 2009. During the third quarter of 2009 we entered into an agreement with ACN Pacific Pty Ltd., a wholly-owned subsidiary of ACN, pursuant to which we will provide digital phone and video VoIP telecommunications services to ACN Pacific. Pursuant to this agreement, ACN Pacific is required to pay us a one-time set-up fee of \$260,000 and will pay us a monthly subscriber-based fee going forward.

Sales to direct consumers decreased by approximately \$0.2 million, or 30%, to approximately \$0.5 million for the three months ended September 30, 2009, from approximately \$0.7 million for the three months ended September 30, 2008. The decrease in consumer revenues was primarily due to a shift in our focus and resources away from our consumer division.

On November 3, 2009, we were informed that the operations of our largest customer had been suspended. In 2008, this customer accounted for approximately 16.5% of our annual gross revenues, and in the third quarter of 2009 this customer accounted for approximately 29% of our gross revenues. At this time we do not know if or when such customer will resume its operations or if, following any such resumption of operations, such customer and we will resume our commercial relationship. The loss of revenue attributable to this customer could have a material adverse effect on our financial condition and results of operations.

Costs and Operating Expenses

Cost of revenues. Cost of revenues increased by approximately \$0.6 million, or 18%, to approximately \$4.0 million, at a 17% gross margin, for the three months ended September 30, 2009, from approximately \$3.4 million, at a 29% gross margin, for the three months ended September 30, 2008. The increase in cost of revenues for the third quarter of 2009 was primarily due to:

- pricing pressures affecting our margins, increasing our termination and network costs for such period by approximately \$0.6 million; and
- a reassessment of our cost allocation due to the reductions in force that occurred during 2008, which contributed an additional \$0.2 million to our cost of revenue.

These were partially offset by a decrease in salaries and related costs of approximately \$0.2 million due to the reductions in force that occurred during 2008.

Research and development expenses. Research and development expenses decreased by approximately \$0.5 million, or 83%, to approximately \$0.1 million for the three months ended September 30, 2009, from approximately \$0.6 million for the three months ended September 30, 2008. As a percentage of revenues, research and development expenses decreased to 2% for the three months ended September 30, 2009, from 13% for the three months ended September 30, 2008, due to the reductions in force that occurred during 2008.

Selling and marketing expenses. Selling and marketing expenses decreased by approximately \$0.4 million, or 67%, to approximately \$0.2 million for the three months ended September 30, 2009, from approximately \$0.6 million for the three months ended September 30, 2008. As a percentage of revenues, sales and marketing expenses decreased to 4% for the three months ended September 30, 2009, from 13% for the three months ended September 30, 2008. This decline was primarily caused by the decrease in sales commissions and salaries expenses resulting from the reductions in force that occurred during 2008.

General and administrative expenses. General and administrative expenses equaled approximately \$0.7 million for both the three months ended September 30, 2009, and the three months ended September 30, 2008, and 15% as a percentage of revenues for both the three months ended September 30, 2009, and for the three months ended September 30, 2008. The reductions in force that occurred during 2008 caused a decrease in general and administrative expenses of approximately \$0.1 million for the three months ended September 30, 2009, which was offset by an increase in legal and professional fees and litigation and other related expenses of approximately \$0.1 million.

Depreciation and amortization. Depreciation and amortization decreased by approximately \$0.3 million, or 60%, to approximately \$0.2 million for the three months ended September 30, 2009, from approximately \$0.5 million for the three months ended September 30, 2008. This was primarily due to amortization of an intangible asset that was recorded as a result of the Go2Call acquisition and write-offs of various fixed assets during 2008, which substantially changed the base value of our fixed assets.

Write-down of Go2Call intangible asset. During the three months ended September 30, 2008, in order to properly adjust the value of the intangible asset associated with an asset we acquired as part of the Go2Call transaction we wrote off approximately \$3.1 million, which represented the entire amount of such asset. No such expenses were recorded for the three months ended September 30, 2009.

Loss from Operations

As a result of the above, operating loss for the three months ended September 30, 2009, was approximately \$0.4 million, a decrease of 90% compared to the operating loss of approximately \$4.1 million for the three months ended September 30, 2008.

Interest Expense, Net

Interest expense, net decreased by approximately \$125,000 to approximately \$32,000 for the three months ended September 30, 2009, from interest income, net of approximately \$93,000 for the three months ended September 30, 2008.

Income Taxes, Net

We accrued net income taxes of approximately \$19,000 for the three months ended September 30, 2009, compared to approximately \$12,000, for the three months ended September 30, 2008. There was no income tax provisions recorded during the three months ended September 30, 2009, since we experienced a net loss for the period.

As of December 31, 2008, we had net operating loss carryforwards, or NOLs, generated in the U.S. of approximately \$80.0 million. Our issuance of common stock to D4 Holdings in February 2009 may constitute an "ownership change", as defined in Section 382 of the Internal Revenue Code, which may result in a loss of a substantial amount of the NOLs we have accrued and our ability to offset income that we may generate in the future. Our ability to use our remaining NOLs could be additionally reduced if we experience any further "ownership change," as defined under Section 382. We have not recorded deferred taxes in respect of the NOLs since it is unlikely that we will be able to utilize these NOLs.

Net Loss

For the three months ended September 30, 2009, we had a net loss of approximately \$0.4 million, compared to a net loss of approximately \$4.0 million for the three months ended September 30, 2008. The decrease in the net loss was due to the factors set forth above.

Results of Operations - Nine Months Ended September 30, 2009, Compared to Nine Months Ended September 30, 2008

Revenues

Revenues for the nine months ended September 30, 2009, totaled \$15.3 million, a decrease of \$0.3 million, or 2%, from \$15.6 million for the nine months ended September 30, 2008. Revenues from our reseller and service provider divisions increased by approximately \$0.4 million, or 3%, to approximately \$13.6 million for the nine months ended September 30, 2009, from approximately \$13.2 million for the nine months ended September 30, 2008. This occurred primarily as a result of an increase in our revenues generated by our largest reseller from zero in the nine months ended September 30, 2008, to approximately \$4.6 million in the nine months ended September 30, 2009, offset by a significant decrease in revenues generated by our smaller resellers during that period. In addition, revenues from our second largest reseller increased from approximately \$2.4 million in the nine months ended September 30, 2008, to approximately \$3.0 million in the nine months ended September 30, 2009.

Within the reseller business itself, we made a decision in the first quarter of 2009 to focus on servicing fewer, larger resellers rather than more, smaller resellers. Consequently, our two largest resellers accounted for approximately \$7.6 million, or approximately 63%, of the revenues generated from our reseller division in the first nine months of 2009. This represented approximately 49% of our total revenue for the nine months ended September 30, 2009. By comparison, in the first nine months of 2008 our two largest resellers accounted for approximately \$3.7 million, or approximately 35%, of the revenue generated from our reseller division, which equaled approximately 25% of our total revenue for first nine months ended September 30, 2008.

Revenues generated by our service provider division decreased by approximately \$1.3 million, or 45%, to \$1.6 million for the nine months ended September 30, 2009, from \$2.9 million for the nine months ended September 30, 2008, primarily due to the termination of our agreements with two customers. This included the termination of our agreement with our largest service provider client, which had accounted for revenue of approximately \$1.8 million in the first nine months of 2008 (representing approximately 11% of our gross revenues for that period). Simultaneously, the total revenue generated from our other service provider clients declined by approximately \$0.5 million during this period. During the third quarter of 2009 we entered into an agreement with ACN Pacific Pty Ltd., a wholly-owned subsidiary of ACN, pursuant to which we will provide digital phone and video VoIP telecommunications services to ACN Pacific. Pursuant to this agreement, ACN Pacific is required to pay us a one-time set-up fee of \$260,000 and will pay us a monthly subscriber-based fee going forward.

Sales to direct consumers decreased by approximately \$0.6 million, or 27%, to approximately \$1.6 million for the nine months ended September 30, 2009, from approximately \$2.2 million for the nine months ended September 30, 2008. The decrease in consumer revenues was primarily due to a shift in our focus and resources away from our consumer division.

Costs and Operating Expenses

Cost of revenues. Cost of revenues increased by approximately \$1.5 million, or 13%, to approximately \$12.8 million, at a 16% gross margin, for the nine months ended September 30, 2009, from approximately \$11.3 million, at a 28% gross margin, for the nine months ended September 30, 2008. The increase in cost of revenues for the first nine months of 2009 was primarily due to:

- pricing pressures affecting our margins, which led to an increase in our termination and network costs for such period by approximately \$1.9 million;
- a reassessment of our cost allocation due to the reductions in force that occurred during 2008, which contributed an additional \$0.6 million to our cost of revenue; and
- the incurrence of \$0.3 million of expenses for devices shipped to new customers.

These were partially offset by a decrease in salaries and related costs of approximately \$0.8 million due to the reductions in force that occurred during 2008 and one-time credits for settlement of old accounts payable of approximately \$0.1 million.

We also had the following one-time expenses during the first nine months of 2008 that affected our cost of revenues during that period:

- customer support costs of approximately \$0.2 million for our joip offering; and
- a restatement of revenues related to previous years of \$0.2 million, which was included in cost of sales for the nine months ended September 30, 2008.

Research and development expenses. Research and development expenses for the nine months ended September 30, 2009, were approximately \$0.3 million, which represented a decrease of approximately 90% compared to research and development expenses of approximately \$2.9 million for the nine months ended September 30, 2008. As a percentage of revenues, research and development expenses decreased to 2% for the nine months ended September 30, 2009, from 19% for the nine months ended September 30, 2008. The decrease was mainly a result of the reductions in force that occurred during the second half of 2008, since salaries and related expenses are the main components that comprise this item.

Selling and marketing expenses. Selling and marketing expenses decreased by approximately \$2.2 million, or 71%, to approximately \$0.9 million for the nine months ended September 30, 2009, from approximately \$3.1 million for the nine months ended September 30, 2008. As a percentage of revenues, selling and marketing expenses decreased to 6% for the nine months ended September 30, 2009, from 20% for the nine months ended September 30, 2008. This decline was primarily caused by the decrease in sales commissions and salaries expenses resulting from the reductions in force that occurred during 2008.

General and administrative expenses. General and administrative expenses increased by approximately \$0.7 million, or 37%, to approximately \$2.6 million for the nine months ended September 30, 2009, from approximately \$1.9 million for the nine months ended September 30, 2008. As a percentage of revenues, general and administrative expenses increased to 17% for the nine months ended September 30, 2009, from 12% for the nine months ended September 30, 2008. This was primarily due to an increase in legal and professional fees and litigation and other related expenses of approximately \$0.6 million partially offset by a decrease in general and administrative expenses of \$0.3 million caused by the reductions in force that occurred during 2008.

Depreciation and amortization. Depreciation and amortization decreased by approximately \$0.8 million, or 53%, to approximately \$0.7 million for the nine months ended September 30, 2009, from approximately \$1.5 million for the nine months ended September 30, 2008. This was primarily due to amortization of an intangible asset that was recorded as a result of the Go2Call acquisition and write-offs of various fixed assets during 2008, which substantially changed the base value of our fixed assets.

Restructuring costs. We did not record any reorganization expenses for the nine months ended September 30, 2009. For the nine months ended September 30, 2008, we recorded reorganization expenses totaling approximately \$1.0 million. These were primarily one-time costs related to reductions in force. In addition, we subleased our New York office for the remaining term of the lease and have accrued the shortfall due to the landlord and legal costs and broker fees associated with the sublease.

Write-down of Go2Call intangible asset. During the first nine months of 2008, in order to properly adjust the value of the intangible asset associated with an asset we acquired as part of the Go2Call transaction we wrote off approximately \$3.6 million, which represented the entire amount of such asset. No such expenses were recorded for the nine months ended September 30, 2009.

Deferred revenue restatement. For the three months ended March 31, 2008, we took a \$200,000 charge as an initial estimate to our deferred revenue liability. As part of a continued review of the deferred revenue liability, we determined that such amount was insufficient and adjusted it during the three months ended June 30, 2008, by an additional \$396,000. The total amount recorded for the nine months ended September 30, 2008 was \$596,000. We did not take any such charge for the nine months ended September 30, 2009.

Loss from Operations

As a result of the above, operating loss for the nine months ended September 30, 2009, was approximately \$2.1 million, a decrease of 79% compared to the operating loss of approximately \$10.1 million for the nine months ended September 30, 2008.

Interest Expense, Net

Interest expense, net decreased by approximately \$87,000 to approximately \$64,000 for the nine months ended September 30, 2009, from interest income, net of approximately \$23,000 for the nine months ended September 30, 2008.

Income Taxes, Net

Income taxes, net increased by approximately \$2,000, or 7%, to approximately \$29,000 for the nine months ended September 30, 2009, from income taxes, net of approximately \$27,000 for the nine months ended September 30, 2008.

Net Loss

For the nine months ended September 30, 2009, we had a net loss of approximately \$2.1 million, compared to a net loss of approximately \$10.1 million for the nine months ended September 30, 2008. The decrease in the net loss was due to the factors set forth above.

Liquidity and Capital Resources

Since our inception in 1996, we have incurred significant operating and net losses. As of September 30, 2009, we had an accumulated deficit of approximately \$175 million.

As of September 30, 2009, we had cash and cash equivalents of approximately \$2.4 million and restricted cash and short-term investments of approximately \$0.3 million, or a total of \$2.7 million in cash and restricted cash, which represented an increase of \$0.6 million as compared to \$2.1 million in cash and restricted cash as of December 31, 2008. On February 12, 2009, we issued to D4 Holdings 39,000,000 shares of our common stock for an aggregate purchase price of \$1,170,000, payable in cash, offset by \$0.1 million of costs incurred in the transaction. The increase in cash and restricted cash was primarily due to the net cash of approximately \$1.1 million provided by the stock issuance to D4 Holdings in the first quarter of 2009, as reduced by our losses during the first nine months of 2009.

During the nine months ended September 30, 2009, we generated negative cash flow from operating activities of approximately \$0.5 million compared with negative cash flow from operating activities of approximately \$4.1 million during the nine months ended September 30, 2008.

Our capital expenditures during the nine months ended September 30, 2009, decreased to \$142,000 compared to \$327,000 for the nine months ended September 30, 2008. Due to the level of investment we had made in capital expenditures in previous years, we were only required to make minimal investments to maintain our overall utilization of our existing domestic and international network infrastructure. During the first nine months of 2009 we had proceeds of approximately \$156,000 from sales of equipment, which resulted in a capital gain of \$86,000.

We obtained our funding from our utilization of the remaining proceeds from our initial public offering, offset by positive or negative cash flow from our operations, and most recently from the sale of shares of our common stock to D4 Holdings in February 2009. These proceeds are maintained as cash, restricted cash and short term investments. As of September 30, 2009, we had negative working capital equal to approximately \$1,127,000 as well as negative stockholders' equity equal to approximately \$412,000. Management believes that we will continue to experience losses and increased negative working capital and negative stockholders' equity in the near future and may not be able to return to positive cash flow before we require additional cash. There can be no assurance that we will be able to raise such additional capital on favorable terms or at all. If additional funds are raised through the issuance of equity securities, our existing stockholders will experience significant further dilution. There can be no assurances that our financial condition will improve in the foreseeable future. As a result of the foregoing factors, there is substantial doubt about our ability to continue as a going concern.

Item 4T. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures.

Each of our principal executive officer and principal financial officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report on Form 10-Q, has concluded that, based on such evaluation, and as a result of the material weaknesses described below, our disclosure controls and procedures were not adequate and effective to ensure that material information required to be disclosed by us in the reports that we file and submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

(b) Changes in Internal Controls.

During the course of 2008 we effected a series of reductions in force that caused the number of our employees to drop from 148 as of December 31, 2008, to 44 as of September 30, 2009. As a result of this sharp decline our ability to ensure a proper segregation of duties amongst different employees was severely curtailed. This had a material effect on our internal controls over financial reporting, and resulted in material weaknesses relating primarily to:

- recording of revenues and deferred revenues, primarily in the authorization, monitoring and segregation of duties over our billing system; and
- recording of cost of revenues, primarily in the authorization, monitoring and segregation of duties over our route purchasing system.

In addition, our existing network security policies failed to identify certain unauthorized traffic on our network. We have revised such policies and taken steps to increase our network security to prevent a recurrence of the unauthorized use of our network.

With the assistance of an outside consulting firm that provides Sarbanes-Oxley Act compliance services and advice, we have begun working on updating our internal control documentation and, where needed, improving our internal controls in order to ensure they function effectively and in compliance with all regulatory requirements.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

There have been no material changes to our Legal Proceedings as described in Item 1 of our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2009, as filed with the SEC, except as described below.

On June 9, 2009, Centre One served a Disclosure of Asserted Claims and Infringement Contentions, in which it accused certain of our VoIP services, in addition to Verizon VoiceWing, of infringing Patent '668. Centre One identified our Hosted Consumer VoIP Solutions, Consumer Group Global Internet Phone Service, and Reseller Programs as allegedly infringing.

On June 22, 2009, the United States Patent and Trademark Office, or the "PTO", granted a request by Verizon Long Distance LLC to reexamine Patent '668, and issued a non-final office action rejecting all but two of the 37 claims of Patent '668 as not patentable. On July 8, 9, and 10, 2009, we and the other defendants moved to stay the litigation in the Eastern District of Texas pending the PTO's reexamination of Patent '668. Centre One opposed the stay motions on July 10, 2009. The court has not yet ruled on the stay motions.

On July 14, 2009, Verizon Long Distance, and on August 13, 2009, Vonage and we, filed Invalidation Contentions seeking to invalidate under 35 U.S.C. §102 and/or §103 all of the claims of Patent '668 asserted over prior patents and publications of third parties not disclosed to the PTO at the time that Patent '668 was granted.

On August 24, 2009, Centre One amended at the PTO 12 of the 21 claims it had asserted in the litigation. On September 18, 2009, Centre One moved to amend its Infringement Contentions to withdraw the claims it had amended at the PTO and to assert two additional claims of infringement. The other defendants and us agreed to the withdrawn claims but opposed Centre One's attempt to assert new claims. The court has not yet ruled on the motion.

We are not a party to any other material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which we are a party or of which any of our property is the subject.

Item 1A. Risk Factors.

There have been no material changes to our risk factors as described in Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2008, as filed with the SEC on April 15, 2009, and our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2009, as filed with the SEC on August 14, 2009, except to the extent additional factual information disclosed in this Quarterly Report on Form 10-Q relates to such risk factors and except as described below.

We are substantially dependent upon a few material customers, and any significant decline in our sales to those customers could have a material adverse effect on our revenues.

In 2008, one customer accounted for approximately 16.5% of our annual gross revenues. In the third quarter of 2009, this customer accounted for approximately 29% of our gross revenues and another customer accounted for approximately 21% of our gross revenues. We have no long-term agreements with these customers, and we have no assurance that they will continue to purchase services from us in the future. On November 3, 2009, we were informed that the operations of our largest customer had been suspended. At this time we do not know if or when such customer will resume its operations or if, following any such resumption of operations, such customer and we will resume our commercial relationship. Any significant decline in our sales to, or our ability to collect accounts receivables from, these customers could have a material adverse effect on our business, results of operations and financial condition. In addition, because we have recently begun focusing on servicing fewer, larger reseller customers rather than many, smaller reseller customers, it is probable that our dependence upon a few material customers will increase in the future.

In addition, during 2008 a different customer accounted for approximately 10.9% of our gross revenues; in the fourth quarter of 2008 this customer accounted for approximately 9.7% of our gross revenues. In January 2009, we received notice from this customer that no later than May 15, 2009, our service provider contract would be terminated pursuant to the terms of the agreement. Accordingly, we will not receive any more revenue as a result of this agreement, which could have a material adverse effect on our business, results of operations and financial condition.

Our computer systems and operations may be vulnerable to security breaches.

We believe that the secure transmission of confidential information over the Internet, such as credit card numbers, is essential in maintaining user confidence in our services. Although we have developed systems and processes that are designed to protect consumer information and prevent fraudulent credit card transactions, unauthorized use of our network and other security breaches, our computer infrastructure is potentially vulnerable to physical or electronic computer viruses, break-ins and similar disruptive problems and security breaches that could cause interruptions, delays or loss of services to our users. We rely on licensed encryption and authentication technology to effect secure transmission of confidential information, including credit card numbers. It is possible that advances in computer capabilities or new technologies could result in a compromise or breach of the technology we use to protect user transaction data. A party that is able to circumvent our security systems could misappropriate proprietary information, cause interruptions in our operations or utilize our network without authorization. Security breaches also could damage our reputation and expose us to a risk of loss, litigation and possible liability. While we have experienced isolated instances of unauthorized use of our network, and have responded to such events by taking steps to increase our network security, we cannot guarantee you that our security measures will prevent security breaches.

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

We held our Annual Meeting of Stockholders on August 6, 2009. At the meeting the following matters were submitted to a vote of our stockholders, and the results were as follows:

(1) Seven Directors were elected for a term of one year each, to serve until our next annual meeting of stockholders and until their successors are duly elected and qualified, as follows:

- | | |
|--------------------------|---|
| (i) Robert Stevanovski: | 49,296,471 votes for; 573,587 votes withheld; |
| (ii) Anthony Cassara: | 49,300,872 votes for; 569,186 votes withheld; |
| (iii) Lior Samuelson: | 48,638,369 votes for; 1,231,689 votes withheld; |
| (iv) David Stevanovski: | 49,296,471 votes for; 573,587 votes withheld; |
| (v) Gregory Provenzano: | 49,298,922 votes for; 571,136 votes withheld; |
| (vi) J. Lyle Patrick: | 49,544,813 votes for; 325,245 votes withheld; and |
| (vii) Brian Fitzpatrick: | 49,542,362 votes for; 327,696 votes withheld. |

(2) The proposal to approve the adoption of the 2009 Stock Incentive Plan was approved by the following vote: 39,878,508 votes for; 1,024,003 votes against; and 17,137 abstentions.

(3) The proposal to approve an amendment to our Amended and Restated Certificate of Incorporation to eliminate our dual class common stock structure was approved by the following vote: 40,867,422 votes for; 39,649 votes against; and 12,577 abstentions.

(4) The proposal to approve an amendment to our Amended and Restated Certificate of Incorporation to increase the number of authorized shares of Common Stock was approved by the following vote: 48,228,701 votes for; 1,623,752 votes against; and 17,605 abstentions.

(5) The ratification of the appointment of Brightman Almagor & Co., a member firm of Deloitte & Touche, as our independent auditors for the fiscal year ending December 31, 2008, was approved by the following vote: 49,702,110 votes for; 114,080 votes against; and 53,868 abstentions.

Item 6. Exhibits.

See Exhibit Index on page 21 for a description of the documents that are filed as Exhibits to this Quarterly Report on Form 10-Q or incorporated by reference herein.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.

DELTATHREE, INC.

Date: November 12, 2009

By: /s/ Effi Baruch
Name: Effi Baruch
Title: Interim Chief Executive Officer and President, Senior Vice
President of Operations and Technology
(Principal Executive Officer)

Date: November 12, 2009

By: /s/ Ziv Zviel
Name: Ziv Zviel
Title: Chief Financial Officer and Treasurer
(Principal Financial Officer)

EXHIBIT INDEX

Exhibit Number	Description
3.1	Certificate of Amendment to the Company's Amended and Restated Certificate of Incorporation (incorporated by reference from our Quarterly Report on Form 10-Q for the three months ended June 30, 2009).
10.1*	General Terms, dated as of July 29, 2009, by and between the Company and ACN Pacific Pty Ltd.
10.2	Master Service Agreement, dated as of October 9, 2009, between the Company and OJO Service (incorporated by reference from our Current Report on Form 8-K filed on October 16, 2009).
10.3	Amendment No. 2 to Executive Employment Agreement between the Company and Effi Baruch, dated as of October 20, 2009 (incorporated by reference from our Current Report on Form 8-K filed on October 26, 2009).
31.1*	Certification of the Chief Executive Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Chief Financial Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of the Chief Executive Officer, as adopted pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of the Chief Financial Officer, as adopted pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Filed herewith.

GENERAL TERMS

ACN PACIFIC PTY LTD
ABN 85 108 535 708
Level 11, 1 Pacific Hwy, North Sydney
Australia

DELTATHREE, INC.
419 Lafayette Street
New York, N.Y. 10003
U.S.A.

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1 AGREEMENT TO SUPPLY THE SERVICE

- 1.1 Subject to the terms and conditions set forth in the Agreement, deltathree will provide you each Service or Individual Service for its Committed Term.
- 1.2 The Agreement comprises:
- (a) each relevant Service Description, including Pricing Schedule;
 - (b) the General Terms;
 - (c) each relevant Service Level Agreement;
 - (d) each Order;
 - (e) the Operations Manual; and
 - (f) any other document the parties hereto shall agree to from time to time and which they agree shall form a part of the Agreement.
- 1.3 If any of the documents listed in clause 1.2 above is inconsistent with one or more of the others, then the terms and conditions of the documents will prevail in the order set out in clause 1.2 above, unless it is specifically agreed otherwise in writing referencing this clause 1.3.

2 THE SERVICE

- 2.1 deltathree will supply each Service from its Service Start Date.
- 2.2 Each party will reasonably co-operate with the other party to allow deltathree to establish and supply each Service to you safely and efficiently. This includes following deltathree's reasonable requests to provide deltathree's Personnel with safe and prompt access to the Premises and your Personnel, equipment, data and information.

3 EQUIPMENT

- 3.1 You will supply to End Users (at your sole expense) the equipment at their premises which they require to use the Service ("CPE").
- 3.2 You will provide deltathree with working samples of the CPE and all reasonably requested technical information regarding the CPE and deltathree will ensure that its Service is compatible with and provides full functionality using the CPE, subject to clause 3.3 below.
- 3.3 Where any incompatibility or lack of functionality of the Service arises from a fault with the CPE or the CPE not functioning in accordance with the CPE samples and CPE technical information provided to deltathree, then deltathree is not responsible or liable for such incompatibility or lack of functionality.

4 MAINTENANCE

4.1 deltathree may conduct regularly scheduled maintenance and emergency maintenance on the deltathree Network. deltathree will use all reasonable endeavours to conduct regularly scheduled maintenance outside normal business hours (in the time zones in which the End Users are located) but may not always be able to do so. When conducting regularly scheduled maintenance deltathree will use reasonable endeavours to provide you with 7 Business Days' notice. D3 will notify you of emergency maintenance as soon as practicable.

5 SERVICE CHARGES

5.1 You will pay the charges for each Service as set out in the Agreement without any withholding (except as contemplated by clauses 7 and 8 below), deduction or set-off and in accordance with any applicable provisions of the Service Description.

5.2 deltathree may charge you an additional amount to service, modify, repair or replace a Service or any equipment as a result of an Excluded Event (except an Intervening Event).

5.3 If agreed between the parties, deltathree may charge you an additional amount for installation, maintenance or other services which you request deltathree to provide outside normal business hours (in the time zones in which the End Users are located) or additional amount for installation.

5.4 deltathree may round up any charge to the nearest cent.

6 INVOICES, PAYMENT AND ADDITIONAL CHARGES

6.1 deltathree may charge you:

- (a) for any equipment you purchase from deltathree or its Personnel, on or after delivery;
- (b) for any installation charges, prior to or after installation;
- (c) for variable charges, in arrears;
- (d) for recurring or fixed charges, in arrears; and
- (e) otherwise as set out in the Agreement.

6.2 deltathree's billing period is monthly except where otherwise provided under the Agreement.

6.3 Subject to clause 7 (Billing Disputes), you will pay each invoice within 30 days from the date of the invoice.

6.4 deltathree will endeavour to include on your invoice all charges for the relevant billing period. As this may not always occur, deltathree may include unbilled charges in any later invoice(s) issued up to 90 days after the date the unbilled charge accrued.

- 6.5 If you do not pay any amount invoiced by 30 days from the date of invoice (except any amount which is validly disputed under clause 7) the amount due under that invoice shall accrue interest at a rate of 2% per annum above the Reserve Bank of Australia target cash rate from time to time, calculated on the daily balance of the unpaid amount from the due date until the date of payment in full. In the event that such rate exceeds the maximum default rate permitted by applicable law, the default rate shall be at the highest rate permitted by applicable law. This is an independent obligation which applies before and after judgment. You will also pay deltathree's expenses in recovering payment from you.
- 6.6 Neither you nor deltathree shall have the right to defer, adjust, set off or withhold any payment due under these General Terms.
- 6.7 You will pay all charges incurred in respect of each Service in Australian Dollars, by direct transfer into the bank account or accounts advised in writing by deltathree from time to time. Where deltathree elects a bank account outside Australia, deltathree must ensure that such account is able to accept Australian Dollars and deltathree shall be responsible for all fees, charges and taxes associated with the transfer of the funds to the overseas account as well as any currency conversion charges should deltathree, or deltathree's bank, convert Australian Dollars to another currency.
- 7 BILLING DISPUTES**
- 7.1 You may dispute an amount invoiced by deltathree but only if you do so in accordance with this clause 7.
- 7.2 Except to the extent you dispute particular charges and raise a valid billing dispute as to an invoice received from deltathree, you will be deemed to have agreed that such invoice is fully accurate, valid and payable (and you must pay the undisputed amount included in the invoice in accordance with clause 6.3 above).
- 7.3 To raise a valid billing dispute, you must:
- (a) If an agreed procedure is set out in the deltathree Billing Dispute Resolution Process document, follow that procedure; and
 - (b) do so within 190 days of the date of the relevant deltathree invoice, except in the case of fixed recurring charges where you must do so within 60 days of the date of the relevant deltathree invoice.
- 7.4 You may only commence or continue legal proceedings alleging that any charge or invoice is incorrect if you have acted in accordance with clause 7.3 and legal proceedings have been properly issued and served on deltathree within 24 months of the date of the relevant invoice.
- 7.5 If, after a billing dispute is concluded you are to pay an amount to deltathree, then you must pay that amount no later than the date ("**Payment Date**") which is 30 days after determination of the dispute. If you do not do so, deltathree may charge you interest on the relevant amount in accordance with clause 6.7 from the Payment Date.

7.6 If, after a billing dispute is concluded deltathree is to pay an amount to you then it will do so by crediting you with that amount on its next and subsequent invoices until the full amount has been credited or, if the contract has terminated for any reason, no later than the Payment Date.

8 TAXES

8.1 Charges specified in the Agreement do not include any GST. You will pay deltathree an additional amount equal to the GST payable on the charges, any non-monetary consideration or on a supply or any component of supply made or to be made in connection with a Service or the charges.

8.2 In some cases the Agreement may specify a charge followed by another amount in parentheses or as 'without GST' and 'with GST'. In those cases, the specified charge or 'without GST' amount is exclusive of GST and the amount in parentheses or specified as 'with GST' is:

- (a) the charge inclusive of GST at the rate in effect at the date of the Agreement; and
- (b) included by way of information only, and its inclusion does not limit your obligation under clause 8.1 to pay the GST exclusive charge together with an additional amount equal to the GST at the rate applicable from time to time.

8.3 If you are required by law to deduct or withhold Taxes from a payment to deltathree, then you may make those deductions or withholdings (or both). However, you will give deltathree a receipt for each payment and you will increase your payment to deltathree by the amount necessary to ensure deltathree receives the full amount which it would have received if no deduction or withholding had been made.

8.4 If clause 8.3 applies, then deltathree will on request by you apply for any credit or rebate to which it may be entitled in connection with the deduction or withheld Tax. deltathree will refund to you any credit or rebate received, up to the amount of the increase made by you under clause 8.3.

8.5 deltathree will ensure it is properly registered for GST and will issue you with a valid tax invoice in respect of each taxable supply.

8.6 Terms used in this clause 8 which are defined in the *A New Tax System (Goods and Services Tax) Act 1999* (Cth) have the meaning given to them in that Act.

9 NON-EXCLUSIVE RELATIONSHIP

9.1 deltathree and you agree that the relationship between the parties is non-exclusive and you may obtain Services and Individual Services from suppliers other than deltathree and deltathree may provide Services and Individual Services to purchasers other than ACN Pacific.

10 PRIVACY AND PERSONAL INFORMATION

- 10.1 deltathree may collect, use and disclose Personal Information provided by you for purposes relating to the supply of a Service described in the Agreement, or for purposes that would be reasonably expected as part of the supply of the Service.
- 10.2 deltathree must not disclose Personal Information provided by you to any person other than its Personnel, except deltathree may disclose Personal Information to deltathree's suppliers (so that deltathree can supply a Service) or as permitted by the Privacy Laws or other laws.
- 10.3 You must not disclose Personal Information provided by deltathree to any person other than your Personnel, except as permitted by the Privacy Laws or other laws.
- 10.4 Both parties must take all reasonable steps to protect Personal Information provided by the other party from misuse and loss and from unauthorised access, modification or disclosure.
- 10.5 Both parties agree to handle Personal Information obtained from the other party in accordance with the Privacy Laws.
- 10.6 In your privacy collection statements you must notify the natural persons from whom you collect Personal Information that their Personal Information may be provided to your suppliers for the purpose of supplying a Service.
- 10.7 For the purposes of this clause a reference to a "party" or "supplier" includes its agents and contractors.

11 COMPLIANCE WITH LAWS OR REGULATOR DIRECTIONS

- 11.1 deltathree and you will comply with all applicable federal, state, and local government rules which have the force of law, including, without limitation, all statutes, laws, ordinances and regulations, and all other laws of any other jurisdiction applicable to the performance of such party's obligations under this Agreement ("Laws") in connection with the exercise of its rights and performance of its obligations under this Agreement.
- 11.2 You are solely responsible for:
- (a) ensuring you have all necessary consents, licences and authorisations to resupply each Service to End Users, including consents and authorisations from End Users, Suppliers and other carriage service providers; and
 - (b) informing your End Users that, where a Service is a Carriage Service, deltathree may be required to intercept communications over the Service and may also monitor your usage of the Service and communications sent over it.
- 11.3 deltathree is solely responsible for:
- (a) ensuring it has all necessary consents, licences and authorisations to supply each Service to you, including consents and authorisations from Regulators, Suppliers and other carriage service providers;

- (b) ensuring that, where a Service is a carriage service, deltathree is able to intercept and monitor communications over the Service where required by a law enforcement agency; and
 - (c) ensuring that it and each Service it supplies complies with all relevant Laws and relevant industry codes (whether registered with a Regulator or not) (“**Industry Codes**”), the directions of a Regulator and other regulatory instruments.
- 11.4 deltathree acknowledges, without representing or warranting, that it is a carriage service provider under the *Telecommunications Act 1997* and, in certain instances, you rely on deltathree in order to comply with Laws and Industry Codes, and agrees that (except as you expressly instruct) it shall not commit any act or omission that places you in violation of any Law or Industry Code.
- 11.5 In using a Service, you and deltathree will comply with directions of a Regulator and each party will use its best efforts to assist the other party in complying with directions of a Regulator.
- 11.6 It is a condition of this Agreement that neither you nor deltathree will use, nor attempt to use, a Service and you will use all reasonable endeavours to prevent your End Users using or attempting to use, a Service:
- (a) to violate any Law or to infringe another person’s rights;
 - (b) to expose either party to liability;
 - (c) to transmit, publish or communicate material which is defamatory, offensive, abusive, indecent, menacing or unwanted; or
 - (d) in any way which damages, interferes with or Interrupts the Service, the deltathree Network or a Supplier Network.
- 11.7 deltathree may ask you to stop, or ask you to stop your End-Users, acting or failing to act in a manner which deltathree reasonably believes is contrary to clauses 11.2 or 11.6. You will as soon as reasonably practicable (but in any case within two Business Days) comply with any such request. If you do not, then deltathree may take any steps reasonably necessary to ensure compliance with clauses 11.2 or 11.6 or the request.
- 11.8 Notwithstanding anything to the contrary in this Agreement, if a material breach of this agreement by either party relates to compliance with laws or Regulator directions then both parties will mutually review the breach and seek commercially reasonable methods of overcoming the breach if possible. Both parties will then evaluate the options, and if there is a way to overcome the breach utilizing commercially reasonable methods, then (i) both parties will initiate such actions, and (ii) upon written agreement by the parties, an equitable adjustment for any delays and changes in scope or quality of services caused by such breach shall be made by the defaulting party if such change materially affects the time or quality of performance or the cost of the Services to be performed under this Agreement. If the parties fail to cure such a material breach of Laws or Regulator directions within sixty (60) days after written notice of non-compliance, the non-defaulting party may terminate the Agreement or affected Service by providing written notice to the other party.

12 YOUR RIGHT TO TERMINATE

12.1 You may, without liability, terminate the Agreement or one or more Services or Individual Services:

- (a) at any time by giving at least 120 days' notice to deltathree;
- (b) by giving 30 days notice in the event that you and deltathree cease to be Related Corporations;
- (c) immediately by giving deltathree notice if:
 - (i) except as set forth in clause 11.8, deltathree breaches a fundamental term of the Agreement and that breach is not capable of remedy or that breach is capable of remedy and deltathree does not remedy that breach as soon as possible but in all circumstances no later than 14 days after you give deltathree notice requiring the breach to be remedied;
 - (ii) deltathree suffers an Insolvency Event;
 - (iii) that Service or Individual Service which is to be terminated is not being supplied and that non-supply has continued for more than 10 Business Days as a result of an Intervening Event having occurred; or
 - (iv) that Individual Service which is to be terminated is no longer required because of the termination or cancellation of an End User Service.

13 DELTATHREE'S RIGHT TO SUSPEND OR TERMINATE

13.1 deltathree may, without liability, Suspend a Service or one or more Individual Services:

- (a) if deltathree reasonably believes that you or any other person (except deltathree) has committed or is about to imminently commit fraud in connection with either the Service or the Individual Service and you fail to take steps (to deltathree's satisfaction) to ensure that fraud does not continue or recur within 48 hours after deltathree gives you notice requiring you to do so;
- (b) by giving you notice to the extent necessary for deltathree to comply with an order, instruction or request of a Regulator, an emergency services organisation or any other competent authority;
- (c) immediately by giving you notice if you have not complied with a notice from deltathree issued in accordance with clause 11.7 relating to that Service or Individual Service;
- (d) immediately to the extent the Service is affected by an Emergency; or

- (e) immediately to the extent it is necessary to allow deltathree or a Supplier to repair, maintain or service any part of the deltathree Network or a Supplier Network used to supply the Service or the Individual Service.

13.2 deltathree may, without liability, terminate the Agreement or Suspend or terminate one or more Services or Individual Services:

- (a) At any time by giving at least 120 days' notice to you;
- (b) immediately if any amount owing to deltathree is not paid by its due date (as specified in the Agreement, the relevant invoice or as notified by deltathree), deltathree gives you notice requiring payment of that amount (which deltathree may not give in respect of an amount which is validly disputed in accordance with clause 7 (Billing Disputes) until after deltathree has determined the billing dispute) and you fail to pay that amount in full within 30 days after deltathree gives you that notice;
- (c) except as set forth in clause 11.8, you breach clause 11.2 or any other fundamental term of the Agreement (other than a breach which separately gives rise to rights under this clause 13.2) and that breach is not capable of remedy, or
- (d) except as set forth in clause 11.8, you breach clause 11.2 or any other fundamental term of the Agreement (other than a breach which separately gives rise to rights under this clause 13.2), that breach is capable of remedy and you do not remedy that breach as soon as possible but in all circumstances no later than 14 days after deltathree gives you notice requiring the breach to be remedied;
- (e) immediately if you suffer an Insolvency Event;
- (f) immediately if that Individual Service which is to be terminated is not being supplied and that non-supply has continued for more than 10 Business Days as a result of an Intervening Event having occurred; or
- (g) if deltathree is otherwise entitled to do so under this Agreement.

14 CONSEQUENCES OF SUSPENSION

14.1 If a Service or an Individual Service is Suspended in accordance with the Agreement, then you will not be liable to pay usage based charges for the Service or the Individual Service while it is Suspended, but you will have to pay any other charges arising during suspension if the Service or Individual Service was Suspended as a result of a breach of the Agreement by you or as a result of the occurrence of any of the events set forth in clauses 13.1 (a) or (c) or clauses 13.2(b), (c) or (d).

14.2 If deltathree Suspends or Downgrades a Service or an Individual Service under clause 13.1 (d) and such suspension or Downgrade is not due to an Intervening Event, the period during which the Service or an Individual Service is Suspended will count towards outage time used in calculating service level rebates (if any) applicable to the affected Service or Individual Service.

14.3 deltathree will stop the suspension of a Service or Individual Service as soon as reasonably possible after the reason for that suspension has stopped in the reasonable opinion of deltathree.

15 CONSEQUENCES OF TERMINATION (TRANSITION)

15.1 On Termination you will retain all rights to the affected End Users and Delta 3 will have no rights in relation to the affected End Users except in accordance with the transition provisions in this clause 15.

15.2 On Termination deltathree must not, except in accordance with the transition provisions in this clause 15, solicit any End User in Australia or New Zealand for a period of 2 years. The term "solicit" shall not be deemed to include generalized advertising or marketing by deltathree for customer through mass market media advertisements or other non-targeted means.

15.3 Notice of Termination of the Agreement or all Services provided under the Agreement by either party will commence a period (the "**Transition Period**") during which the parties will cooperate in transitioning all End Users to replacement services provided by you or your designee (the "**Replacement Service**"). deltathree during the Transition Period will create a configuration file for each model of CPE then in use by End Users, which configuration file will point such CPE to the Replacement Service and grant the Replacement Service full access to and control over such CPE, and will deploy such configuration files remotely to End Users over the course of the Transition Period in accordance with the schedule reasonably established by you. As quickly as reasonably practicable during the Transition Period, you will arrange for a Replacement Service, arrange to port End User phone numbers to the Replacement Service and otherwise transition the End Users to the Replacement Service. The Transition Period shall continue until the earlier of the date on which all End Users have been removed from the applicable Service and the date fourteen (14) months following the notice of Termination. This Agreement, including your obligation to pay fees and charges pursuant to this Agreement, will remain in effect throughout the Transition Period.

15.4 At any time and from time to time during a Transition Period, on receipt of a request from you deltathree will, as soon as possible and in any case within 72 Business Hours, provide an up to date copy of all data held by deltathree in relation to the End Users in a format and manner reasonably specified by you plus any other information reasonably requested by you which will assist in the transition of the End Users to Replacement Services.

15.5 Once an End User has been successfully transitioned to a Replacement Service, deltathree must, to the extent permitted by law, delete and permanently remove all copies to data relating to that End User which is in deltathree's custody and control.

15.6 On Termination

- (a) of the Agreement or all Services provided under the Agreement for any reason, each party will (on request by the other party) immediately return or destroy the other person's Confidential Information, except to the extent that it is required by law to retain it;

- (b) of the Agreement for any reason, each person's accrued rights and obligations are not affected and the parts of the Agreement which are by their nature intended to survive Termination of the Agreement will do so.

16 EACH PARTY'S RIGHTS AGAINST THE OTHER

- 16.1 Each party accepts liability to the other in connection with the Individual Services, the Services and the Agreement, but only to the extent provided in this clause 16. Each party excludes any liability (including in negligence) it might otherwise have to the other in connection with this Agreement, the Services or any Individual Service to the extent that such liability is not expressly accepted under this clause 16.
- 16.2 Each party agrees to indemnify, defend and hold the other party harmless for all Loss to the other party arising from personal injury to the other party's Personnel to the extent it is caused directly by the negligence of the first party in connection with the Agreement. The limitation in clause 16.8 does not apply to this clause.
- 16.3 Each party agrees to indemnify, defend and hold the other party harmless for all Loss (up to the value of the damage to the damaged property) arising from damage to the other party's physical property to the extent it is caused directly by the negligence of the first party in connection with the Agreement. The limitation in clause 16.8 does not apply to this clause.
- 16.4 Each party's liability for the other party's Loss (including arising as a result of negligence) under clause 16.2 or 16.3 or, except where clause 17 applies, otherwise in connection with the Individual Services, the Services or the Agreement is reduced to the extent that:
 - (a) a Loss suffered or incurred by the other party could have been avoided or mitigated by reasonable action by that party; and
 - (b) acts or omissions of the other party or its Personnel cause or contribute to that Loss.
- 16.5 deltathree accepts liability to you under the Trade Practices Act and other laws where not to accept such liability would be illegal or would make any part of this clause 16 void or unenforceable. Otherwise, deltathree disclaims and excludes all conditions and warranties implied into the Agreement and limits its liability for any non-excludable conditions and warranties, where permitted by law to do so, to (at deltathree's option) repairing or replacing the relevant goods, resupplying the relevant or equivalent services or, in either case, paying you the cost of doing so.
- 16.6 deltathree accepts liability to you for Loss arising from Interruptions to Individual Services and the Services (including for Interruptions due to negligence) to the extent the Interruptions are not caused or contributed to by Excluded Events, but only:
 - (a) by crediting to you a service rebate, where one is specified in the relevant Service Level Agreement and validly claimed by you in accordance with the Agreement; or

- (b) if there is no service rebate so specified, by (at deltathree's election) repairing or replacing the relevant goods or resupplying any relevant or equivalent services which are capable of being resupplied, or in either case paying you the cost of doing so.

If deltathree credits you with a service rebate, this is your sole remedy for deltathree's acts or omissions leading up to the credit, except to the extent clauses 16.2 and 16.3 apply.

- 16.7 Except for claims under clauses 16.2, 16.3, 17, 18, claims arising from a breach of clause 11.2 and obligations to pay outstanding charges, each party's aggregate liability arising out of this Agreement to the other for Loss suffered or incurred in connection with the Individual Services, the Services or the Agreement is limited to the lesser of (i) the total amounts received by deltathree from you under this Agreement or (ii) AU \$5 million.
- 16.8 Except for claims under clauses 16.2, 16.3 and 17, claims arising from a breach of clause 11.2 and obligations to purchase a Service or Individual Services or pay outstanding charges, each party excludes any liability to the other for any Consequential Loss suffered or incurred in connection with the Individual Services, the Services or with the Agreement (including liability for negligence).
- 16.9 In this clause 16 and clause 17, indemnities, limitations and exclusions in favour of a party are to be construed as indemnities, limitations and exclusions in favour of each Group Company of that party.
- 16.10 For the avoidance of doubt, the terms and conditions set forth in clauses 18.8 and 18.9 apply to the indemnities given in this clause 16.

17 END USERS LIABILITY

- 17.1 deltathree excludes any liability (including in negligence) to your End Users. You agree to indemnify, defend and hold deltathree harmless against any Loss suffered or incurred by deltathree in connection with an End-User claim (including a claim based in negligence) in any way related to an Individual Service, the Services or the Agreement.
- 17.2 For the avoidance of doubt, the terms and conditions set forth in clauses 18.8 and 18.9 apply to the indemnities given in this clause 17.

18 INTELLECTUAL PROPERTY

- 18.1 deltathree may permit you to use deltathree Intellectual Property as part of a Service, as may be set forth in a Service Description. This permission is subject to any conditions which deltathree may impose from time to time and will cease when the relevant Service or this Agreement is terminated. You acknowledge and agree that you will not use deltathree Intellectual Property, except as set out in this Agreement, unless authorised to do so in writing by deltathree.

- 18.2 Except as specifically set out in this Agreement, neither party will obtain any interest in or to the other party's Intellectual Property Rights solely by access to or use of the same related to this Agreement.
- 18.3 Except as permitted in a Service Description, you must:
- (a) not grant a right to any third person, including an End User, to use any deltathree Intellectual Property; and
 - (b) ensure that your End Users do not use or promote deltathree Intellectual Property, the trade marks or names of any other person in conjunction or association with the deltathree Intellectual Property without the prior written consent of deltathree.
- 18.4 You must not, whether by yourself, your directors, servants or agents, during the Committed Term of this Agreement or after its Termination:
- (a) dispute deltathree's, or any deltathree Related Corporations', rights in or ownership of any deltathree Intellectual Property;
 - (b) challenge the validity of a registration in the name of deltathree, or a Related Corporation of deltathree, of deltathree Intellectual Property; or
 - (c) challenge any application by deltathree or a Related Corporation of deltathree for registration of the deltathree Intellectual Property in classes other than those in which that the deltathree Intellectual Property is currently registered.
- 18.5 If you become aware of any possible infringement of deltathree Intellectual Property by you, an End User or any other third party, you must immediately advise deltathree and provide deltathree with all relevant details.
- 18.6 Subject to the terms of this Agreement, you agree to indemnify, defend and hold deltathree and any deltathree Group Company harmless for all Loss arising from any claim or proceeding by any person against any of those indemnified under this clause, where such Loss arose out of your breach of this clause 18 or an infringement, or an alleged infringement, of the Intellectual Property Rights of deltathree which occurred by or as a result of your use or enjoyment of the Services.
- 18.7 deltathree agrees to defend, indemnify and hold you and any ACN Pacific Group Company harmless from and against any claim brought by a third party against you to the extent that the claim includes a claim of any infringement of any Intellectual Property Rights or other proprietary interest of such third party arising from or relating to the deltathree Services or your use, deployment or sale thereof as contemplated by this Agreement; and all Losses relating thereto excluding Consequential Loss. Notwithstanding the foregoing, deltathree shall not be obligated or liable to defend or indemnify ACN Pacific or any ACN Pacific Group Company and shall not be responsible for any Loss related thereto under this Agreement to the extent that any such claim arises from (i) ACN Pacific's or a third party's modification of the deltathree Services without the express written consent of deltathree, (ii) combination of the deltathree Services with services, products, processes or materials not furnished, specified or approved by Deltathree; or (iii) deltathree's use of or adherence to specifications or instructions furnished to deltathree by ACN Pacific to the extent that such specifications or instructions result in infringement.

- 18.8 The indemnified party shall promptly notify the indemnifying party in writing of any claim for which the indemnifying party is responsible under this indemnity obligation (provided that the failure by the indemnified party to provide prompt written notice shall not relieve the indemnifying party from any of its obligations hereunder, except to the extent the indemnifying party is actually prejudiced thereby).
- 18.9 The indemnifying party shall assume, at its expense, the sole defence of the claim through counsel selected by the indemnifying party and shall keep the indemnified party fully informed as to the progress of such defence. Upon reasonable request of the indemnifying party and at the indemnifying party's expense, the indemnified party shall cooperate in the defence of the claim. At its option and expense, the indemnified party may retain or use separate counsel to represent it, including in-house counsel. The indemnifying party shall maintain control of the defence, except that if the settlement of a claim would adversely affect the indemnified party, the indemnifying party may settle the claim as to the indemnified party only with the indemnified party's consent, which consent shall not be withheld or delayed unreasonably. If the indemnified party is required to take any action to enforce its indemnity rights under this Agreement, or to assume the defence of any claim for which it is entitled to receive an indemnity under this Agreement because of the indemnifying party's failure to promptly assume such defence, then the indemnified party may also recover from the indemnifying party any reasonable attorneys' fees (including cost of in-house counsel at market rates for attorneys of similar experience) and other costs of enforcing its indemnity rights or assuming such defence.

19 CONFIDENTIALITY

- 19.1 deltathree and you each agree to keep confidential the other's Confidential Information.
- 19.2 Subject to clause 19.3, deltathree and you will not use or disclose the other's Confidential Information for any purpose, other than to the extent necessary to perform its obligations or exercise its rights under the Agreement. This includes deltathree not disclosing any information relating to your End Users to deltathree Personnel, except to the extent that it is necessary to do so to supply a Service to you, or for you to resupply a Service to your End Users.
- 19.3 For clarity, deltathree may refer to you as a customer of deltathree in deltathree press releases, or in deltathree marketing, sales or financial material or reports.
- 19.4 The obligations of confidentiality in this clause 19 do not apply to the extent disclosure is required by a court of competent jurisdiction or other governmental authority or as otherwise required by law or the listing rules of a stock exchange, a direction by government authority or a Regulator, or disclosure to professional advisors in connection with the Agreement.

20 INTERVENING EVENTS

- 20.1 If an Intervening Event occurs which prevents you or deltathree (“**Affected Person**”) from performing any of its obligations (other than an obligation to pay money) under this Agreement, then the Affected Person will not be liable for failing to perform that obligation.
- 20.2 The Affected Person will notify the other person promptly of the Intervening Event and use its best efforts to resume performance in accordance with the Agreement as soon as reasonably possible. The other person’s obligations continue during the **Intervening Event**.

21 PUBLIC ADDRESSING IDENTIFIERS

- 21.1 A Service may include one or more identifiers such as a telephone number, IP address or domain name (“**Public Addressing Identifiers**”).
- 21.2 You will comply with the requirements of any Regulator or other body which administers Public Addressing Identifiers.
- 21.3 You acknowledge and agree that:
- (a) deltathree does not control the allocation of Public Addressing Identifiers;
 - (b) deltathree is not liable to you if deltathree is required to change any Public Addressing Identifier as a result of any direction given by a Regulator or other body which administers Public Addressing Identifiers; and
 - (c) on Termination of a Service or any relevant Individual Service, your right to use any related Public Addressing Identifier may cease.

22 ASSIGNMENT, SUBCONTRACTING AND TRANSFER

- 22.1 To the extent they are assignable, either party may assign, delegate or otherwise transfer its rights under the Agreement so long as it has the other party’s prior written consent, which cannot be unreasonably delayed or withheld.
- 22.2 deltathree may perform any of its obligations under the Agreement by arranging for them to be performed by another person, including a Supplier or another deltathree Group Company. If this occurs deltathree remains responsible for its obligations in accordance with this Agreement.
- 22.3 deltathree will continue supplying the Services even if any interest in you, including your business or any of your shares, is transferred to a third party (“**Purchaser**”) provided that:
- (a) you notify deltathree of the details of the proposed transfer, before entering into any binding arrangement to give effect to it;

- (b) you and/or the proposed Purchaser comply with any reasonable requests from deltathree for financial or operational information demonstrating the creditworthiness of the Purchaser;
- (c) you and/or the proposed Purchaser enter into any necessary assignment or novation which deltathree reasonably requests in the circumstances, within 30 days of that request.

23 DISPUTES

- 23.1 This clause applies to any dispute arising under the Agreement except billing disputes (which are handled in accordance with clause 7).
- 23.2 A party must notify the other if it believes a dispute exists and that notice must provide details of the matter in dispute.
- 23.3 After receipt of the notice set out in clause 23.2, the parties will promptly seek to resolve the dispute by escalation within their respect organisations.
- 23.4 If the dispute has not been resolved within 20 Business Days after the notice in clause 23.2 is given either of the parties may refer the dispute for mediation to the Institute of Arbitrators and Mediators Australia.
- 23.5 Except where urgent interlocutory relief is required, a party may not commence legal proceedings in relation to any dispute unless it has complied with this clause 23 and the dispute has not been resolved within 50 Business Days after the notice in clause 23.2 is given.

24 RECORDS & AUDITS

- 24.1 deltathree will maintain complete and accurate records related to the Services provided by deltathree to you, including records of all amounts billable to and payments made by you in accordance with generally accepted accounting principles applicable to U.S. corporations, uniformly and consistently applied in a format that will permit audit.
- 24.2 deltathree will retain such records and reasonable billing detail for a period of at least seven (7) years from the date of final payment for Services.
- 24.3 You may at your sole expense, upon reasonably prior written notice to deltathree, audit during normal business hours the charges invoiced to you relating to the Services, such audit to occur no more frequently than one time per fiscal quarter. deltathree shall have the right to exclude from such inspection any of information that is confidential or proprietary to a third party, in deltathree's reasonable opinion.
- 24.4 deltathree will report minute usage and other relevant information, which shall be provided by deltathree to you, on a daily and monthly basis, as more particularly described in the relevant Service Schedule.

25 PUBLICITY

- 25.1 Neither you nor deltathree shall provide copies of the Agreement, or otherwise disclose the terms of this Agreement, to any third party (other than the parties' lawyers, accountants/auditors, and/or anyone the party is required to disclose it to by law) without the prior written consent of the other party, provided, that no consent will be required for either party to disclose the terms of this Agreement to a potential lender, investor, acquirer or other similar third party, or such third party's lawyers, accountants and advisors, in connection with such third party's due diligence review.
- 25.2 Except as required by law and except as provided in Clause 19.3 above, neither you nor deltathree shall not use the other party's names or any language, pictures, trademarks, service marks or symbols which could imply its identity or endorsement in any:
- (a) written, electronic or oral advertising or presentation; or
 - (b) brochure, newsletter, book, electronic database or other written matter of whatever nature, without such party's prior written consent.

Hereafter the terms in subsections (a) and (b) of this clause 25.2 shall be collectively referred to as "**Publicity Matters**".

- 25.3 The using party will submit to the other party for written approval, prior to publication, all Publicity Matters that mention or display such names, trademarks or service marks, or that contain any symbols, pictures or language from which a connection to said names or marks may be inferred or implied. Such written approval of Publicity Matters required by law shall not be unreasonably withheld or delayed.
- 25.4 Notwithstanding the foregoing, a party may, without obtaining the other party's prior written consent, include the other's name, and a factual description of the work performed under the Agreement on employee bulletin boards and in internal business planning documents and, following the public issuance of the press release referred to in Clause 25.5 below, such information may be included in reports to stockholders, offering memoranda and other securities disclosure documents and whenever necessary to meet legal, accounting or regulatory requirements.
- 25.5 Promptly following the execution of this Agreement by both you and deltathree, either party may issue a press release approved by the other party (such approval shall not be unreasonably withheld. Any press release or public announcement shall be consistent with the need to restrict general public awareness of the role of your vendors in your branded service such as the Services.

26 NO SOLICITATION

- 26.1 During such time as deltathree provides Services to you and for a period of twelve (12) months following the Termination thereof, neither you nor deltathree will, directly or indirectly, solicit to employ or hire any employee of the other party that is directly or indirectly involved in the performance of the Services, without the prior written consent of the other party. The term "solicit to employ" shall not be deemed to include generalized searches or hiring by either Party for employees through media advertisements, employment firms or otherwise.

27 GENERAL

27.1 Every notice under or in connection with the Agreement:

- (a) must be in writing (except where expressly stated otherwise);
- (b) must be addressed as follows (or as otherwise notified from time to time)

Name: ACN Pacific Pty Ltd
Address: Level 11, 1 Pacific Highway, North Sydney,
NSW, Australia, 2060
Fax: +61 2 8214 4111
email: iain.falshaw@acnaustralia.com.au
For the attention of: Iain Falshaw

With a copy (which shall not constitute notice) to: Lloyd Edwards
Lloyd.edwards@acnaustralia.com.au

Name: deltathree, Inc.
Address: 419 Lafayette Street
New York, N.Y. 10003
Fax: (212) 500-4888
email: dan.antebi@deltathree.com
For the attention of: Dan Antebi

With a copy (which shall not constitute notice) to: Peter Friedman, Esq.
peter.friedman@deltathree.com

- (c) must be delivered by hand, or posted by overnight or similar delivery service, or sent by confirmed fax to the number, of the addressee, in accordance with clause 27.1(b); and
 - (i) is taken to be received by the addressee:
 - (ii) (in the case of overnight delivery sent to an address in the same country), on the third day after the date of posting, with written verification of receipt;
 - (iii) (in the case of overnight delivery sent to the address in another country) on the fifth day after the date of posting by airmail with a recognized international delivery service, with written verification of receipt;
 - (iv) (in the case of confirmed fax) at the time of such transmission if sent during normal business hours of the recipient; and
 - (v) (in the case delivery by hand) on delivery,

but if the communications is taken to be received on a day that is not a working day or after 5.00 pm, it is taken to be received at 9.00am on the next working day (“working day” meaning a day that is not a Saturday, Sunday or public holiday and on which banks are open for business generally, in the place to which the communication is posted, sent or delivered).

- 27.2 You will nominate at least two authorised operational contacts and provide any relevant details in relation to them required by deltathree.
- 27.3 If either party has a right arising out of a breach of this Agreement by the other party and does not exercise that right, not exercising that right does not waive:
- (a) that right unless it does so in writing; or
 - (b) its right to insist on performance of that or any other obligation at any other time.
- 27.4 If a provision of the Agreement is void, voidable or unenforceable, it will be severed and the remainder of the Agreement will not be affected.
- 27.5 Each person will pay its own costs and expenses in respect of the Agreement and any agreement or document contemplated by the Agreement or required to give effect to it, but you must pay any stamp duty (including fines) assessed on the Agreement and any agreement or document contemplated by the Agreement or required to give effect to it.
- 27.6 Nothing in the Agreement shall be deemed to have created a relationship of employer and employee, principal and agent, partnership or joint venture between the parties. This Agreement shall not be construed as authority for either party to act on behalf of the other in any agency or other capacity.
- 27.7 The Agreement is governed by the laws applicable in the State of New South Wales and you and deltathree submit to the exclusive jurisdiction of the courts of that State.
- 27.8 The Agreement constitutes the entire agreement between the parties as to its subject matter and supersedes all prior representations and agreements in connection with that subject matter.
- 27.9 The Agreement may only be varied in writing signed by you and deltathree.
- 27.10 The parties intend that the Agreement shall not benefit or create any right or cause of action in, or on behalf of, any person or entity other than the parties to this Agreement and no person or entity other than the parties to the Agreement shall be entitled to rely on the provisions of the Agreement in any action, suit, proceeding, hearing or other forum.
- 27.11 Each Party represents and warrants to the other Party that:
- (a) it has been duly organized and is validly existing and in good standing under the laws of the jurisdiction of its organization;

- (b) it has the full right, power and authority to execute, deliver and perform its obligations under this Agreement;
- (c) its execution of and performance under this Agreement does not and will not violate any applicable existing regulations, rules, statutes or court orders of any local, state or national government agency, court or body of any country or any contract or other agreement to which it is subject;
- (d) its execution and performance under this Agreement does not and will not violate or cause a conflict with or default under any other binding contract or agreement to which it is subject;
- (e) when executed and delivered by it, this Agreement will constitute the legal, valid and binding obligation of it, enforceable against it in accordance with its terms, subject to applicable bankruptcy and other laws that affect the rights of creditors generally; and
- (f) it has obtained, or will obtain, all necessary consents and approvals and any withholding of objection required from any entity, including any governmental authority with respect to the entering into or the performance of this Agreement.

27.12 These General Terms may be executed in counterparts, each of which may be deemed to be an original and both of which together shall constitute one and the same instrument.

27.13 The following rules of interpretation apply to the Agreement, unless the contrary intention appears.

- (a) The expressions "deltathree", "you" or "your" will include their respective successors and permitted assigns and novatees.
- (b) A reference to a person includes a reference to a person, firm, corporation or other legal entity.
- (c) A term which is defined in any part of the Agreement has the same meaning in every other part of the Agreement.
- (d) The singular includes the plural and vice versa.
- (e) A reference to a thing includes any part of that thing.
- (f) Different grammatical forms of the same word have the corresponding meaning.
- (g) A reference to a clause is to a clause in this document, unless otherwise stated.
- (h) Examples or words of inclusion are illustrative only and do not limit the generality of the relevant subject.
- (i) A "reasonable" notice period means a period which is reasonable in the circumstances taking into account technical, operational and commercial issues. For clarity, "reasonable" notice regarding an event may include notice after the event, or no notice at all.

28 **DICTIONARY TO GENERAL TERMS**

28.1 Words in a clause of this Agreement have the meaning given in that clause, the Telecommunications Legislation or in this dictionary as follows.

ACN Pacific means ACN Pacific Pty Ltd, an Australian corporation.

Agreement means the documents set out in clause 1.2 above.

Application means Order.

Business Day means a day (other than a Saturday, Sunday or public holiday) on which banks are open generally for business in Sydney.

Committed Term means, in respect of a Service or Individual Service, the period specified as the "Committed Term", "Term" or the period generally described as the period over which deltathree will supply the Services, as set out in the Order or elsewhere in the Agreement, including variations or extensions of that period however described. The Committed Term, in respect of a Service or Individual Service, commences on the Service Start Date. If there is no period of Committed Term specified in the Application or Agreement, then there will be no period of Committed Term after the Service Start Date.

Confidential Information of a party means all information of that party ("**Owner**") of a confidential nature (whether in written, oral, electronic or other form), which another person ("**Recipient**") first becomes aware, whether before or after the date of the original Order, either through disclosure by the Owner to the Recipient or otherwise through the Recipient's involvement with the Owner. **Confidential Information** includes information regarding the other party's customers, technology, network, trades secrets and all non-public information relating to the current or future business interests, methodology or practices or affairs of either party.

Confidential Information does not include information:

- (a) the Recipient creates (whether alone or jointly with any person) independently of the Owner's Confidential Information or the Recipient knew prior to receiving such information from the Owner;
- (b) that is public knowledge (otherwise than as a result of a breach of confidentiality by the Recipient or any person to whom it has disclosed the information); or
- (c) obtained without restriction as to further disclosure from a third party other than the Owner through no breach of confidentiality by that third party.

For deltathree, "Owner" and "Recipient" includes deltathree and each deltathree Group Company excluding ACN Pacific.

Consequential Loss means:

- (a) loss of revenue, loss of profits, loss of anticipated savings or business, pure economic loss, loss of data, loss of value of equipment (other than cost of repair), loss of opportunity or expectation loss and any other form of consequential, special, indirect, incidental, punitive or exemplary loss or damages; and
- (b) any penalties or fines imposed by a Regulator.

Control (including the correlative terms “*Controls*”, “*Controlled by*”, and “*under common Control with*”) means, with respect to any person, entity or enterprise, the power, directly or indirectly, either to (i) vote a majority of the voting shares or other voting interests in such person, entity or enterprise for the election of directors or other governing body of such person, entity or enterprise or (ii) direct or cause the direction of the management and policies of such person, entity or enterprise, whether through the ownership of voting securities, by contract or otherwise.

CPE has the meaning assigned in clause 3.1.

deltathree means deltathree, Inc., a Delaware corporation.

deltathree Intellectual Property means any material owned, developed or licensed by deltathree or its Personnel, in which deltathree has Intellectual Property Rights.

deltathree Network means any telecommunications network, equipment, facilities or cabling controlled by deltathree.

deltathree Billing Dispute Resolution Process document is the document agreed between the parties from time to time which sets out the billing dispute resolution process for all Services.

Downgrade means any modification to a Service or an Individual Service which reduces the capacity, use or utility of that Service or Individual Service.

Emergency means an actual or potential state of danger requiring immediate action to avoid any Loss, including personal injury or property Loss.

End User means any person to whom you supply an End User Service.

End User Service means the complete retail end-to-end service which you provide to a customer of yours using one or more Individual Services.

Excluded Event means:

- (a) a breach of the Agreement by you,
- (b) an Intervening Event;
- (c) a negligent or fraudulent act or omission of you or any of your Personnel; or
- (d) a failure of any of your equipment.

General Terms means this General Terms.

Group Company of a party means each of that party's Related Corporations other than the other party.

GST has the meaning given in the *A New Tax System (Goods and Services Tax) Act 1999* (Cth).

Individual means a natural person.

Individual Service means each individual service component making up a Service; for example, an individual circuit or connection for a specific End User. For clarity, there may be more than one Individual Service making up a Service.

Insolvency Event means in relation to a person:

- (a) the person proposing to enter, or entering, into any scheme of arrangement (including Chapter 11 type arrangements) between that person and its creditors (except an arrangement for the purposes of a solvent reconstruction);
- (b) a mortgagee entering into possession or disposing of the whole or any part of the assets or business of the person;
- (c) appointment of a receiver, a receiver and manager, a liquidator, a provisional liquidator, an administrator or other like person to the person or to the whole or any part of its assets or business, or the person taking any step to have such a person appointed to itself or the whole or any part of its assets or business;
- (d) the person suspending payment of its debts generally; or
- (e) the person being or becoming insolvent for the purposes of section 95A of the *Corporations Act 2001* (Cth).

Intellectual Property Rights means all industrial and intellectual property rights, including without limitation, registered or unregistered trademarks, patents, copyright, rights in circuit layouts, trade secrets, confidential know how and information and any application or right to apply for registration of any of those rights. Intellectual Property includes the right to have Confidential Information kept confidential.

Interruption in the supply of goods or a service (including a Service and each Individual Service) means a delay in supplying, a failure to supply or an error or defect in the supply of, those goods or that service. (**Interrupt(s)** will be construed accordingly).

Intervening Event affecting a person means any event or circumstance outside that person's reasonable control, and includes fire, storm, flood, earthquake, accident, war, labour dispute (other than a dispute solely between that person and its own staff or staff under its control), materials or labour shortage, the change or introduction of any law or regulation, an act or omission of any Regulator or an act or omission of any third party (including any Supplier) where the act or omission is caused by an event or circumstance outside that third party's reasonable control (including any of the things mentioned in this definition).

Loss means any loss, cost, liability or damage, including reasonable legal costs on a solicitor/client basis and includes Consequential Loss, unless otherwise stated.

Operations Manual means the deltathree / ACN Dispute Resolution Process document and all other service documentation agreed between deltathree and you from time to time to be part of the Operations Manual.

Order means a request for a Service or an Individual Service made in the manner specified in the relevant Service Description.

Personal Information means information or an opinion (including information or an opinion forming part of a database), whether true or not and whether included in material form or not, about an Individual whose identity is apparent, or can reasonably be ascertained, from the information or opinion.

Personnel of a person means that person's employees, agents, contractors or other representatives and, in the case of deltathree, includes the employees, agents, contractors or other representatives of any deltathree Group Company excluding ACN Pacific.

Premises means locations at which deltathree supplies a Service, and locations to which deltathree needs to have access to supply a Service.

Privacy Laws means *Privacy Act 1988* (Cth), the *Telecommunications Act 1997* (Cth) and the *Spam Act 2003* (Cth), each as amended or replaced from time to time.

Regulator means the Australian Communications Authority, the Australian Communications and Media Authority, the Australian Competition and Consumer Commission, Communications Alliance Ltd, the Telecommunications Industry Ombudsman or any other government or statutory body or authority.

Related Corporation of an entity means a body corporate that, directly or indirectly, through one or more intermediaries, Controls, is Controlled by, or is under common Control with such entity.

Service means the service with the options and features requested in the Order or Orders as described in the relevant Service Description, and any related goods (including equipment) and ancillary services which deltathree supplies to you in connection with that service.

Service Delivery Point means the point at which a Service is made available for connection to your equipment or cabling.

Service Description means the part of the Agreement entitled "Service Description" which describes a Service.

Service Option means certain features and characteristics of a Service which may be selected by you and which are described as a 'Service Option' (together with any additional terms on which the Service Option is supplied) in the Service Description or any appendix to the Service Description.

Service Start Date for a Service or an Individual Service means the date on which deltathree starts supplying that Service or Individual Service to you, or is deemed to do so.

Supplier means any supplier of goods or services (including interconnection services) which are used directly or indirectly by deltathree to supply a Service.

Supplier Network means any telecommunications network, equipment, facilities or cabling controlled by a Supplier.

Suspend means suspend, reduce, restrict or limit supply.

Tax means any withholding tax, charge (and associated penalty or interest), rate, duty or impost imposed by any authority at any time but does not include GST, or any tax on income or capital gains.

Telecommunications Legislation means the *Telecommunications Act 1997* (Cth) and the *Telecommunications (Consumer Protection and Service Standards) Act 1999* (Cth), each as amended or replaced from time to time, and Part XIB and Part XIC and related provisions of the Trade Practices Act.

Termination means termination of this Agreement, a Service or an Individual Service, as applicable.

Trade Practices Act means the *Trade Practices Act 1974* (Cth), as amended or replaced from time to time.

General Terms means this document.

You means ACN Pacific.

Signed for and on behalf of ACN Pacific Pty Ltd

By: /s/ Iain Falshaw

Name: Iain Falshaw

Title: Managing Director

Date: July 29, 2009

Signed for and on behalf of deltathree, Inc.

By: /s/ Effi Baruch

Name: Effi Baruch

Title: CEO and President

Date: July 27, 2009

Exhibit 31.1

CERTIFICATION BY PRINCIPAL EXECUTIVE OFFICER

I, Effi Baruch, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of deltathree, Inc. (the "registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 12, 2009

By: /s/ Effi Baruch
Effi Baruch
Interim Chief Executive Officer and President, Senior Vice President of
Operations and Technology

Exhibit 31.2

CERTIFICATION BY PRINCIPAL FINANCIAL OFFICER

I, Ziv Zviel, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of deltathree, Inc. (the "registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 12, 2009

By: /s/ Ziv Zviel
Ziv Zviel
Chief Financial Officer and Treasurer

Exhibit 32.1

CERTIFICATION

**Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, the undersigned officer of deltathree, Inc. (the "registrant") does hereby certify, to such officer's knowledge, that:

- (1) the Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 (the "Form 10-Q") of the registrant 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 Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the registrant.

Date: November 12, 2009

By: /s/ Effi Baruch
Effi Baruch, Interim Chief Executive Officer and President, Senior Vice
President of Operations and Technology

The foregoing certification will not be deemed "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

CERTIFICATION

**Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, the undersigned officer of deltathree, Inc. (the "registrant") does hereby certify, to such officer's knowledge, that:

- (1) the Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 (the "Form 10-Q") of the registrant 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 Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the registrant.

Date: November 12, 2009

By: /s/ Ziv Zviel
Ziv Zviel, Chief Financial Officer and Treasurer

The foregoing certification will not be deemed "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.
