

TUCOWS INC /PA/  
Form 10-K  
March 22, 2011

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

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**FORM 10-K**

**FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO  
SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

(Mark One)

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

For the fiscal year ended December 31, 2010

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
Commission file number 001-32600

**Tucows Inc.**

(Exact Name of Registrant as Specified in Its Charter)

**Pennsylvania**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**23-2707366**  
(I.R.S. Employer  
Identification No.)

**96 Mowat Avenue**  
**Toronto, Ontario, Canada**  
(Address of Principal Executive Offices)

**M6K 3M1**  
(Zip Code)

Registrant's telephone number, including area code: **(416) 535-0123**

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

| Title of Each Class        | Name of Each Exchange on Which Registered |
|----------------------------|---|
| Common stock, no par value | NYSE Amex                                 |

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

(Title of Class)  
None

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

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, 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                       Accelerated filer                       Non-accelerated filer                       Smaller reporting company   
(Do not check if a  
smaller reporting  
company)

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

As of June 30, 2010 (the last day of our most recently completed second quarter), the aggregate market value of the common stock held by non-affiliates of the registrant was \$24.9 million. Such aggregate market value was computed by reference to the closing sale price per share of \$0.64 as reported on the NYSE Amex on such date. For purposes of making this calculation only, the registrant has defined affiliates as including all officers, directors, and beneficial owners of more than ten percent of the common stock of the Company. In making such calculation, the registrant is not making a determination of the affiliate or non-affiliate status of any holders of shares of the registrant's common stock.

The number of shares outstanding of the registrant's common stock as of March 17 2011 was 53,448,441.

### TRADEMARKS, TRADE NAMES AND SERVICE MARKS

Tucows®, Butterscotch®, OpenSRS®, Hover®, YummyNames® and Platypus® are registered trademarks of Tucows, Inc. or its subsidiaries. Other service marks, trademarks and trade names of Tucows, Inc. or its subsidiaries may be used in this Annual Report on Form 10-K (the "Annual Report"). All other service marks, trademarks and trade names referred to in the Annual Report are the property of their respective owners. Solely for convenience, any trademarks referred to in the Annual Report may appear without the ® or TM symbol, but such references are not intended to indicate, in any way, that we or the owner of such trademark, as applicable, will not assert, to the fullest extent under applicable law, our or its rights, or the right of the applicable licensor, to these trademarks.

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**TUCOWS INC.  
ANNUAL REPORT ON FORM 10-K  
For Fiscal Year Ended December 31, 2010**

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**Information Concerning Forward-Looking Statements**

This Annual Report on Form 10-K contains, in addition to historical information, forward-looking statements by us with regard to our expectations as to financial results and other aspects of our business that involve risks and uncertainties and may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "may," "should," "anticipate," "believe," "plan," "estimate," "expect" and "intend," and other similar expressions are intended to identify forward-looking statements. The forward-looking statements contained in this report include statements regarding, among other things, the number of new, renewed and transferred-in domain names, the competition we expect to encounter as our business develops and competes in a broad range of Internet services, the effectiveness of our intellectual property protection, including our ability to license proprietary rights to network partners and to register additional trademarks and service marks, our belief that the market for domain name registration will trend upward gradually, our belief that it is more likely than not that net deferred assets will be realized; our intent to continue acquisitions of previously owned domain names, the effect of a potential gTLD expansion by the Internet Corporation for Assigned Names and Numbers ("ICANN") on the number of domains we register and related revenues; and our belief that, by increasing the number of applications and services we offer, we will be able to generate higher revenues. These statements are based on management's current expectations and are subject to a number of uncertainties and risks that could cause actual results to differ materially from those described in the forward-looking statements. Many factors affect our ability to achieve our objectives and to successfully develop and commercialize our services including:

Our ability to continue to generate sufficient working capital to meet our operating requirements;

Our ability to maintain a good working relationship with our vendors and customers;

The ability of vendors to continue to supply our needs;

Actions by our competitors;

Our ability to achieve gross profit margins at which we can be profitable;

Our ability to attract and retain qualified personnel in our business;

Our ability to effectively manage our business;

Our ability to obtain and maintain approvals from regulatory authorities on regulatory issues;

Pending or new litigation; and

Factors set forth herein under the caption "Item 1A Risk Factors".

This list of factors that may affect our future performance and financial and competitive position and the accuracy of forward-looking statements is illustrative, but it is by no means exhaustive. Accordingly, all forward-looking statements should be evaluated with the understanding of their inherent uncertainty. All forward-looking statements included in this document are based on information available to us as of the date of this document, and we assume no obligation to update these cautionary statements or any forward-looking statements. These statements are not guarantees of future performance.

We qualify all the forward-looking statements contained in this Annual Report on Form 10-K by the foregoing cautionary statements.



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**PART I**

**ITEM 1. BUSINESS**

**Overview**

Our mission is to provide simple useful services that help people unlock the power of the Internet. We accomplish this by reducing the complexity our customers' experience as they acquire, deliver or use Internet services such as domain name registration, email and other Internet services.

Our primary distribution channel is a global network of more than 11,000 resellers in over 100 countries who typically provide their customers, the end-users of the Internet, with a critical component for establishing and maintaining an online presence. Our primary focus is serving the needs of this network of resellers by providing superior services, easy-to-use interfaces, proactive and attentive customer service, reseller-oriented technology and agile design and development processes. We seek to provide superior customer service to our resellers by anticipating their business needs and technical requirements. This includes providing easy-to-use interfaces that enable resellers to quickly and easily integrate our services into their individual business processes, and offering brandable end-user interfaces that emphasize simplicity and visual appeal. We also provide "second tier" support to our resellers by email and phone in the event resellers experience issues or problems with our services. In addition, our Network Operating Center provides proactive support to our resellers by monitoring all services and network infrastructure to address deficiencies before customer services are impacted.

We believe that the underlying platforms for our services are some of the most mature, reliable and functional reseller-oriented provisioning and management platforms in our industry, and we continue to refine, evolve and improve these platforms for both resellers and end-users.

To assist us in forecasting growth and to help us monitor the effectiveness of our operational strategies, we categorize our revenue into the following services:

OpenSRS, our wholesale service, manages over ten million domain names, under its accreditation by the Internet Corporation for Assigned Names and Numbers, or ICANN, as well as names Tucows manages for other registrars under their own accreditations; millions of mailboxes and tens of thousands of digital certificates through a network of over 11,000 web hosts, Internet service providers, or ISPs, and other resellers around the world.

Platypus, our billing service, provides ISPs with an industry-specific solution for billing, service provisioning and customer account management.

Hover, our retail service, offers services similar to those of OpenSRS to consumers and small businesses.

YummyNames, our domain portfolio service, manages tens of thousands of domain names, most of which generate advertising revenue and many of which we offer for resale via our reseller network and other channels. Included in the YummyNames domain portfolio are over 42,000 domains that allow over two-thirds of Americans to purchase a domain or email address based on their name.

Butterscotch, our content service, operates two advertising-supported websites, butterscotch.com and tu cows.com, which provide content to help consumers overcome the complexity of modern technology and the Internet, in the form of over 4,000 videos and over 385,000 software and mobile listings and articles. Additionally, Butterscotch provides custom video production services for technology manufacturers and ISPs.

Our business model is characterized by non-refundable, up-front payments, which lead to recurring revenue and positive operating cash flow. We are an ICANN-accredited registrar and manage over ten million domains under our ICANN accreditation, as well as names we manage for other registrars under their own accreditations.

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**Net Revenues**

*OpenSRS*

We derive revenue from our reseller network by providing them with reseller services that comprise (a) domain service, (b) email service and (c) other services. Other services primarily consist of secure sockets layer, or SSL, certificates and also include blogware and website building tools that are used by our resellers to create bundles of Internet services for their end-users along with billing solutions for ISPs.

OpenSRS Domain Service

Historically, our OpenSRS domain service has constituted the largest portion of our business and encompasses all of our services as an accredited registrar related to the registration, renewal, transfer and management of domain names. In addition, this service fuels other revenue categories as it often is the initial service for which a customer will engage us, enabling us to follow on with other services and allowing us to add to our domain portfolio by purchasing names registered through us upon their expiration. We also provide resellers with the ability to sell personal names. This service allows resellers the opportunity to sell email addresses based on our domain portfolio of surname domain names.

As of December 31, 2010, we offer registration services for the generic top-level domain ("gTLDs") .com, .net, .org, .info, .name, .biz, .tel, .mobi and .asia and for the country code top-level domains ("ccTLDs") .at, .au, .be, .bz, .ca, .co, .cc, .ch, .cn, .de, .dk, .es, .eu, .fr, .in, .it, .li, .me, .mx, .nl, .tv, .uk, .ws, and .us.

With respect to the sale of domain registrations, our pricing structure for domain names provides visibility into the various fees that make up the cost of a domain name by breaking out the cost of the registry and ICANN fees separately from our management fee. Effective July 2010, registry fees for the .com and .net registrations supplied by our largest registry supplier, Verisign, were increased by an additional 7%. This increase in registry fees, in accordance with our pricing policy, was passed on to our customers at cost. The management fee provides our resellers with access to our provisioning and management tools to enable them to register and administer domain names and access to additional services like WHOIS privacy and DNS services; enhanced domain name suggestion tools and access to our Premium Domain name services. We earn fees in connection with each new, renewed and transferred-in registration and from providing provisioning services to resellers and registrars on a monthly basis. Domain registrations are generally purchased for terms of one to ten years, with a majority having a one-year term. Except for certain large customers with whom we have negotiated alternative arrangements, payments for the full term of service, or billed revenue, is received at the time of activation of service. All fees received in connection with domain name registration are non-refundable, and where appropriate, are recorded as deferred revenue and recognized as earned ratably over the term of provision of service. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the quarters and the year.

OpenSRS Email Service

We derive revenue from our hosted email service through our global distribution network. Our email service is offered on a per account, per month basis, and provides resellers with a reliable, scalable "white label" hosted email solution that can be customized to their branding and business model requirements. The email service also includes spam and virus filtering on all accounts. End-users can access the email service via a full-featured, multi-language AJAX-enabled web interface, a WAP mobile interface, or through traditional desktop email clients, such as Microsoft Outlook or Apple Mail, using IMAP or POP/SMTP and 2GB of email storage.

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We earn fees for email services when such services are activated. Email services are generally purchased monthly and, at month-end, are either deducted on a pre-authorized basis from reseller's deposit account, or are invoiced.

*Other OpenSRS Services*

We derive revenue from other services primarily from provisioning SSL certificates. In addition, we provision blogware and website building tools that are used by our resellers to create bundles of Internet services for their end-users, as well as the provision of billing, provisioning and customer care software solutions to ISPs through our Platypus billing software.

We earn fees from such services when a service is activated. These services are generally purchased for terms of one month to three years. Platypus software is generally purchased for terms of one month to one year. Payments for services are for the full term of all services at the time of activation of service, are non-refundable and, where appropriate, are recorded as deferred revenue and recognized as earned ratably over the service term. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the quarters and the year.

*YummyNames*

We derive revenue from our portfolio of domain names by displaying advertising on the domains and by making them available for sale or lease. In addition we display advertising on "parked pages" within OpenSRS. Parked pages are domain names registered with us that do not yet contain an active website. When a user types one of these domain names into a web browser, they are presented with dynamically generated links that are pay-per-click advertising. Every time a user clicks on one of these links, it generates revenue for us through our partnership with third-parties who provide syndicated pay-per-click advertising.

Portfolio names are sold through our premium domain name service, auctions or in negotiated sales. The size of our domain name portfolio varies over time, as we acquire and sell domains on a regular basis to maximize the overall value and revenue generation potential of our portfolio. In evaluating names for sale, we consider the potential foregone revenue from pay-per-click advertising, as well as other factors. The name will be offered for sale if, based on our evaluation, the name is deemed non-essential to our business and management believes that deriving proceeds from the sale is strategically more beneficial to the Company.

Portfolio names that have been acquired from third-parties or through acquisition are included as intangible assets with indefinite lives on our consolidated balance sheet.

In addition, we also offer the same services to our customers, allowing them to make available names registered by them for monetization on a similar basis. For customer names, we earn a referral fee for premium names or names sold or leased, and participate on a revenue share basis for names offered through our pay-per-click advertising program.

We recognize revenue from these services, net of any fees payable to resellers or customers, immediately upon completion of the service, or in the case of advertising revenue, on a monthly basis once the advertising has been served.

*Hover*

We derive revenues from the providing and managing Internet services, on a retail basis, to consumers and small businesses through our Hover.com website. These services include domain registration and other Internet services such as email and personalized email through our portfolio of surname-based domain names, as well as an easy-to-use interface that allows users to connect domain



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names to websites and email addresses through a unique DNS forwarding system. Depending on the service offered, we typically receive fees for our services.

Our customers generally purchase services for terms of one to ten years, with a majority of services purchased for a one-year term. Certain services are also offered on a monthly basis. Payments for the full term of all services, or billed revenue, are received at the time of service activation and, where appropriate, are recorded as deferred revenue and recognized as earned ratably over the term of provision of service. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during quarterly and annual periods.

*Butterscotch*

We also generate advertising and other revenue through two ad-supported content sites, butterscotch.com and tu cows.com.

Butterscotch.com derives revenue from banner and text advertising on the site, as well as from video advertising and product placement within the videos that make up the bulk of the site. In addition, revenue is earned through custom video production for technology manufacturers and Internet services customers.

Tu cows.com advertising revenue is generated from third-party advertisers and from software developers who rely on us as a primary source of distribution. Software developers use our Author Resource Center to submit their products for inclusion on our site and to purchase promotional placement of their software. Software developers may also purchase other promotional services on a cost-per-click or flat rate basis. Software developers are able to promote their software through advertising services including keyword search placements, banners, promotional placements, expedited reviews and premium data services. Revenue is also generated from companies that contract with us to provide them with co-branded content.

Advertising and other revenue is recognized ratably over the period in which it is presented. To the extent that we do not meet the minimum number of post-presentation impressions that we guarantee to customers, we defer recognition of the corresponding revenues until the guaranteed impressions are achieved. Custom video production revenue is recognized on acceptance of the completed video by the customer.

**Intellectual Property**

We believe that we are well positioned in the wholesale domain registration and email markets due in part to our highly-recognized "Tu cows" and "OpenSRS" brands and the respect they confer on us as a defender of end-user rights and reseller friendly approaches to doing business. We were among the first group of thirty-four registrars to be accredited by ICANN, in 1999 and we remain active in Internet governance issues.

Our success and ability to compete depend on our ability to develop and maintain the proprietary aspects of our brand name and technology. We rely on a combination of trademark, trade secret and copyright laws, as well as contractual restrictions to protect our intellectual property rights.

We have registered the Tu cows trademark in the United States, Canada and the European Union and we register additional service marks and trademarks as appropriate and where such protection is available.

We seek to limit disclosure of our intellectual property by requiring all employees and consultants with access to our proprietary information to commit to confidentiality, non-disclosure and work-for-hire agreements. All of our employees are required to sign confidentiality and non-use agreements, which provide that any rights they may have in copyrightable works or patentable

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technologies accrue to us. Before entering into discussions with potential vendors and partners about our business and technologies, we require them to enter into a non-disclosure agreement. If these discussions result in a license or other business relationship, we also generally require that the agreement containing the parties' rights and obligations include provisions for the protection of its intellectual property rights.

**Customers**

The majority of the customers to whom we provide Reseller Services are generally either web hosts or ISPs. A small number are consultants and designers providing our services to their business clients. Our Retail Services customers are a very broad mix of consumers, small businesses and corporations.

No customer represented more than 10% of our consolidated revenues in any of the last three fiscal years.

While web hosts and ISPs are capitalizing on the growth in Internet usage and the demand for new services, they also face significant competition from numerous other service providers with competitive or comparable offerings. This has led such web hosts and ISPs to focus on core competencies, as such resellers are increasingly seeking to outsource non-core services. Outsourcing enables these resellers to better focus on customer acquisition and retention efforts by eliminating the need to own, develop and support non-core applications in-house.

**Seasonality**

During the summer months and certain other times of the year, such as major holidays, Internet usage often declines. As a result, many of our services (OpenSRS, Hover and Butterscotch) may experience reduced demand.

For example, our experience shows that new domain registrations and traffic on our download site decline during the summer months and around the year-end holidays. Seasonality may also affect advertising, which may have a slight impact on both the content group and the domain name portfolio's advertisement-based revenue. These seasonal effects could cause fluctuations in our financial results as well as the content site's performance statistics reported and measured by leading Internet audience measurement services such as comScore.

**Competition**

Our competition may be divided into the following groups:

Retail-oriented domain registrars such as GoDaddy, Network Solutions and *Register.com* who compete with our Resellers and our own retail operations for end-users.

Wholesale-oriented domain registrars, such as eNom, Wild West Domains (a division of GoDaddy) and Melbourne IT, who market services to resellers such as our customers.

Wholesale Email Service providers, such as Google, Yahoo!, Microsoft, Bluetie and MailTrust.

Ad-supported content providers, such as CNET's *Download.com*.

We expect to continue to experience significant competition from the competitors identified above and, as our business develops, we expect to encounter competition from other providers of Internet services. Service providers, Internet portals, web hosting companies, email hosting companies, outsourced application companies, country code registries and major telecommunication firms may broaden their services to include services we offer.

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We believe the primary competitive factors in our Reseller Services are:

Providing superior customer service by anticipating the technical requirements and business objectives of resellers and providing them with technical advice to help them understand how our services can be customized to meet their particular needs.

Providing cost savings over in-house solutions by relieving resellers of the expense of acquiring and maintaining hardware and software and the associated administrative burden.

Enabling resellers to better manage their relationships with their end-users.

Facilitating scalability through an infrastructure designed to support millions of transactions across millions of end-users.

Providing superior technology and infrastructure, consisting of industry-leading software and hardware that allow resellers to provide these services to their customers without having to make substantial investments in their own software or hardware.

Although we encounter pricing pressure in many markets in which we compete, we believe the effects of that pressure are mitigated by the fact that we deliver a high degree of value to our resellers through our business and technical practices. We believe our status as a trusted supplier also allows us to mitigate the effects of this type of competition. We believe that the long-term relationships we have made with many resellers results in a sense of certainty that would not be available to those resellers through a competitor.

**Employees**

As of December 31, 2010, we had approximately 150 full-time employees. None of our employees are currently represented by a labor union. We consider our relations with our employees to be good.

**Corporate Information**

Tucows Inc. was incorporated under the laws of the Commonwealth of Pennsylvania in November 1992 under the name Infonautics, Inc. In August 2001, we completed our acquisition of Tucows Inc., a Delaware corporation, and we changed our name from Infonautics, Inc. to Tucows Inc. Our principal executive offices are located in Toronto, Ontario, Canada and we have offices in the United Kingdom and the United States of America.

**Executive Officers of the Registrant**

The following table sets forth the names, ages and titles of persons currently serving as our executive officers.

| Name              | Age | Title                                       |
|-------------------|-----|---|
| Elliot Noss       | 48  | President and Chief Executive Officer       |
| Michael Cooperman | 59  | Chief Financial Officer                     |
| David Woroeh      | 48  | Executive Vice President, Sales and Support |

Elliot Noss has served as our President and Chief Executive Officer since May 1999 and served as Vice President of Corporate Services for Tucows Interactive Limited, which was acquired by Tucows in May 1999, from April 1997 to May 1999.

Michael Cooperman has served as our Chief Financial Officer since January 2000. From October 1997 to September 1999, Mr. Cooperman was the Chief Executive Officer of Archer Enterprise Systems Inc., a developer of sales force automation software.

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David Woroch has served as our Executive Vice President, Sales and Support since June 3, 2009 and served as our Vice President Sales and Support since July 2001. From March 2000 to July 2001, Mr. Woroch served as our Director of Sales for North America. Before joining us, Mr. Woroch spent 13 years at IBM Canada in a variety of roles including sales, marketing, finance and strategic planning.

**Investor Information**

The public may read and copy any materials we file with the Securities and Exchange Commission, or SEC, at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549 on official business days during the hours of 10:00 am to 3:00 pm. The public may obtain information on the operation of the Public Reference Room by calling 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements and other information regarding issuers that file electronically at <http://sec.gov>.

Our web site address is [tucowsinc.com](http://tucowsinc.com). We make available through our web site, free of charge, copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC.

The information on the web site listed above is not and should not be considered part of this Annual Report on Form 10-K and is not incorporated by reference in this document.

We were incorporated in the Commonwealth of Pennsylvania in November 1992. Our executive offices are located at 96 Mowat Avenue, Toronto, Ontario, Canada M6K 3M1. Our telephone number is (416) 535-0123.

**ITEM 1A. RISK FACTORS**

*Our business faces significant risks. Some of the following risks relate principally to our business and the industry and statutory and regulatory environment in which we operate. Other risks relate principally to the securities markets and ownership of our stock. The risks described below may not be the only risks we face. Additional risks that we do not yet know of or that we currently think are immaterial may also impair our business operations. If any of the events or circumstances described in the following risk factors actually occur, our business, financial condition or results of operations could suffer, and the trading price of our common stock could decline.*

**Risks Related to Our Business and Industry**

***We may not be able to maintain or improve our competitive position and may be forced to reduce our prices because of strong competition in the market for Internet services generally and domain name registration, in particular, which we expect will continue to intensify.***

The market for Internet services generally and domain registrations in particular is intensely competitive and rapidly evolving as participants strive to protect their current market share and improve their competitive position, and we expect competition to intensify in the future. Most of our existing competitors are also expanding the variety of services that they offer. These competitors include, among others, domain name registrars, website design firms, website hosting companies, Internet service providers, Internet portals and search engine companies, including Google, Microsoft, Network Solutions, VeriSign and Yahoo!. Competitors like Microsoft, Google and Yahoo!, as well as other large Internet companies, have the ability to offer these services for free or at a reduced price as part of a bundle with other service offerings. If these companies decide to devote greater resources to the development, promotion and sale of these new products and services, greater numbers of individuals and businesses may choose to use these competitors as their starting point for creating an

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online presence and as a general platform for running their online business operations. In particular, VeriSign may in the future decide to offer additional services that compete with our domain name registration services or other services. If VeriSign were to become a competitor of ours in our core business areas, VeriSign would likely enjoy a number of competitive advantages, including its position as the largest registry, as well as superior financial and operational resources and customer awareness within our industry.

In addition, other large competitors, in an attempt to gain market share, may also offer aggressive price discounts on the services they offer. These pricing pressures may require us to match these discounts in order to remain competitive, which would reduce our margins, or potentially cause us to lose customers altogether who decide to purchase these discounted services.

We also face significant competition from other existing registrars and the continued introduction of new registrars in the domain registration industry. As of March 17, 2011, ICANN reflects approximately 970 accredited competitive registrars on their website, including our Company, to register domains in one or more of the gTLD's compared to approximately 950 at March 1, 2010. Not all of these accredited registrars are operational. There are relatively few barriers to entry in this market and the continued introduction of competitive registrars and Service Providers into the domain registration industry and the rapid growth of some competitive registrars and service providers who have already entered the industry may make it difficult for us to maintain our current market share. Some of these registrars may have longer operating histories, greater name recognition, particularly in international markets, or greater resources than us. We expect that competition will increase in the near term and that our primary long-term competitors may not yet have entered the market. As a result, we may not be able to compete effectively.

As our business model is premised upon selling multiple services through our resellers, we have competed aggressively to attract new clients and retain existing customers. As a result of these actions, our average selling prices have fallen and we may be required, by marketplace factors or otherwise, to reduce, perhaps significantly, the prices we charge for our domain registration and related products and services. The decline in our average selling price has partially offset the impact of increased transaction volume on our revenue and profitability. The likelihood of further declines in our selling price will increase if our competitors who charge these reduced fees are able to maintain customer service comparable to ours. We may face continued pricing pressure in order to remain competitive, which would adversely impact our revenues and profitability. While we anticipate that the number of new, renewed and transferred-in domain registrations will incrementally increase, volatility in the market could result in our customers turning to other registrars, thereby impairing growth in the number of domains under our management and our ability to sell multiple services to such customers. Since our strategy is to expand the services we provide our customers, if we are unable to maintain our domain registrations, our ability to expand our business may be adversely effected.

***Each registry and the ICANN regulatory body impose a charge upon the registrar for the administration of each domain registration. If these fees increase, this may have a significant impact upon our operating results.***

Each registry typically imposes a fee in association with the registration of each domain. For example, effective July 1, 2010, the VeriSign registry increased the fee for each .com registration from a \$6.86 fee to a \$7.34 fee for each annual .com registration. ICANN charges a \$0.18 fee for each domain name registered in the TLDs that fall within its purview. We have no control over these agencies and cannot predict when they may increase their respective fees. In terms of the current registry agreement between ICANN and Verisign that was approved by the U.S. Department of Commerce on November 30, 2006, VeriSign will continue as the exclusive registry for the .com gTLD through at least November 30, 2012 and is entitled to increase the fee it receives for each .com domain name once in either 2011 or 2012 by up to seven percent of the current fee. In terms of our pricing policy, these

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increases will be passed through to our resellers, while other registrars may choose to absorb them. If such cost increases act as a deterrent to registration, we may find that our profits are adversely impacted by these third-party fees.

***We rely on our network of resellers to renew their domain registrations through us and to distribute our services, and if we are unable to maintain these relationships or establish new relationships, our revenues will decline.***

The growth of our business depends on, among other things, our resellers' renewal of their customers' domain registrations through us. Resellers may choose to renew their domains with other registrars or their registrants may choose not to renew and pay for renewal of their domains. This may reduce our resellers' number of domain name registration customers which in turn would drive up their customer acquisition costs and harm our operating results. If resellers decide, for any reason, not to renew their registrations through us, it may in turn reduce the market to which our resellers could market our other higher-margin services, thereby further impacting our revenue and profitability and harming our operating results.

***We believe that companies operating on the Internet are facing a period of consolidation. In addition, some of our resellers may decide to seek ICANN accreditation. Both of these situations could reduce the number of our active resellers, in which case our revenues may suffer.***

If any of our competitors merge with one another, they will present a stronger combined force in the market and may attract the business of both existing and prospective resellers. Resellers may opt to build their own technical systems and seek ICANN accreditation in order that they may process domain applications themselves. If a number of our customers decide to pursue this option, our sales will decrease.

***Our failure to secure agreements with country code registries or our subsequent failure to comply with the regulations of the country code registries could cause customers to seek a registrar that offers these services.***

The country code top-level domain, or ccTLD, registries require registrars to comply with specific regulations. Many of these regulations vary from ccTLD to ccTLD. If we fail to comply with the regulations imposed by ccTLD registries, these registries will likely prohibit us from registering or continuing to register domains in their ccTLD. Any failure on our part to offer domain registrations in a significant number of ccTLDs or in a popular ccTLD would cause us to lose a competitive advantage and could cause resellers to elect to take their business to a registrar that does offer these services.

***Our standard agreements may not be enforceable, which could subject us to liability.***

We operate on a global basis and all of our resellers must execute our standard agreements that govern the terms of the services we provide to our customers. These agreements contain provisions intended to limit our potential liability arising from the provision of services to our resellers and their customers, including liability resulting from our failure to register or maintain domains properly, from downtime or poor performance with respect to our Internet services, or for insecure or fraudulent transactions pursuant to which we have issued SSL certificates. As most of our customers purchase our services online, execution of our agreements by resellers occurs electronically or, in the case of our terms of use, is deemed to occur because of a user's continued use of the website following notice of those terms. We believe that our reliance on these agreements is consistent with the practices in our industry, but if a domestic, foreign or international court were to find that either one of these methods of execution is invalid or that key provisions of our services agreements are unenforceable, we could be subject to liability that has a material adverse effect on our business or we could be required to change our business practices in a way that increases our cost of doing business.

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***Regulation could reduce the value of Internet domain names or negatively impact the Internet domain acquisition process, which could significantly impair the value attributable to our acquisitions of Internet domain names.***

The acquisition of expiring domain names for parked page commercialization, the sale of names or acquisition of names for other uses, involves the registration of thousands of Internet domain names, both in the United States and internationally. We have and intend to continue to acquire previously-owned Internet domain names that have expired and have, following the period of permitted reclamation by their prior owners, been made available for sale. The acquisition of Internet domain names generally is governed by federal or international regulatory bodies. The regulation of Internet domain names in the United States and in foreign countries is subject to change. Regulatory bodies could establish additional requirements for previously-owned Internet domain names or modify the requirements for holding Internet domain names. As a result, we might not acquire or maintain names that contribute to our financial results in the same manner as we currently do. Because certain Internet domain names are important assets, a failure to acquire or maintain such Internet domain names could adversely affect our financial results and our growth. Any impairment in the value of these important assets could cause our stock price to decline.

***We have presence in the hosted messaging and email market, which is a volatile business.***

Factors that are likely to contribute to fluctuations in our operating results from provisioning hosted email services include:

the demand for outsourced email services;

our ability to attract and retain customers and provide customer satisfaction;

the ability to upgrade, develop and maintain our systems and infrastructure and to effectively respond to the rapid technological changes in the email market;

the budgeting and payment cycles of our existing and potential customers;

the amount and timing of operating costs and capital expenditures relating to expansion of the email service; and

the introduction of new or enhanced services by competitors.

In order to succeed in the hosted email business, our email product must remain competitive. We believe that some of the competitive factors affecting the market for hosted email services include:

breadth of platform features and functionality of our offering and the sophistication and innovation of our competitors;

scalability, reliability, performance and ease of expansion and upgrade;

ease of integration with customers' existing systems; and

flexibility to enable customers to manage certain aspects of their systems and leverage outsourced services in other cases when resources, costs and time to market reasons favor an outsourced offering.

We believe competition will continue to be strong and further increase as our market attracts new competition, current competitors aggressively pursue customers, increase the sophistication of their offerings and as new participants enter the market. Many of our current and

potential competitors have longer operating histories, larger customer bases, greater brand recognition in the business and greater financial, marketing and other resources than we do. Any delay in our development and delivery of new services or enhancement of existing services would allow our competitors additional time to improve their product offerings and provide time for new competition to develop and market



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messaging services. Increased competition could result in pricing pressures, reduced operating margins and loss of market share, any of which could cause our financial results to decline.

*If we are unable to maintain our relationships with our customers our revenue may decline.*

Our network of resellers are our principal source for distributing services. We also rely on our resellers to market, promote and sell our services. Our ability to increase revenues in the future will depend significantly on our ability to maintain our reseller network, to sell more services through existing resellers and to develop our relationships with existing resellers by providing customer and sales support and additional products. Resellers have no obligations to distribute our services and may stop doing so at any time. If we are not able to maintain our relationships with resellers, our ability to distribute our services will be harmed, and our revenue may decline.

*Disputes over registration of domain names, the activities of our reseller's customers or the content of their websites could subject us to liability and could negatively affect the public's perception of our corporate image.*

As a registrar of domain names services, we may be subject to potential liability for illegal activities by our reseller's customers on their websites. We provide an automated service that enables users to register domain names. We do not monitor or review, nor does our accreditation agreement with ICANN require that we monitor or review, the appropriateness of the domain names we register for our customers or the content of their websites, and we have no control over the activities in which these customers engage. While we have policies in place to terminate domain names or to take other action if presented with evidence of illegal conduct, customers could nonetheless engage in prohibited activities without our knowledge.

Several bodies of law may be deemed to apply to us with respect to various customer activities. Because we operate in a relatively new and rapidly evolving industry, and since our industry is characterized by rapid changes in technology and in new and growing illegal activity, these bodies of laws are constantly evolving. Some of the laws that apply to us with respect to customer activity include the following:

The Communications Decency Act of 1996, or CDA, generally protects online service providers, such as Tucows, from liability for certain activities of their customers, such as posting of defamatory or obscene content, unless the online service provider is participating in the unlawful conduct. Notwithstanding the general protections from liability under the CDA, we may nonetheless be forced to defend ourselves from claims of liability covered by the CDA, resulting in an increased cost of doing business.

The Digital Millennium Copyright Act of 1998, or DMCA, provides recourse for owners of copyrighted material who believe that their rights under U.S. copyright law have been infringed on the Internet. Under this statute, we generally are not liable for infringing content posted by third parties. However, if we receive a proper notice from a copyright owner alleging infringement of its protected works by web pages for which we provide hosting services, and we fail to expeditiously remove or disable access to the allegedly infringing material, fail to post and enforce a digital rights management policy or a policy to terminate accounts of repeat infringers, or otherwise fail to meet the requirements of the safe harbor under the statute, the owner may seek to impose liability on us.

Although established statutory law and case law in these areas to date generally have shielded us from liability for customer activities, court rulings in pending or future litigation may serve to narrow the scope of protection afforded us under these laws. In addition, laws governing these activities are unsettled in many international jurisdictions, or may prove difficult or impossible for us to comply with in some international jurisdictions. Also, notwithstanding the exculpatory language of these bodies of law, we may be embroiled in complaints and lawsuits which, even if ultimately resolved in our favor,

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add cost to our doing business and may divert management's time and attention. Finally, other existing bodies of law, including the criminal laws of various states, may be deemed to apply or new statutes or regulations may be adopted in the future, any of which could expose us to further liability and increase our costs of doing business.

Domain name registrars also face potential tort law liability for their role in wrongful transfers of domain names. The safeguards and procedures we have adopted may not be successful in insulating us against liability from such claims in the future. In addition, we face potential liability for other forms of "domain name hijacking," including misappropriation by third parties of our network of customer domain names and attempts by third parties to operate websites on these domain names or to extort the customer whose domain name and website were misappropriated. Furthermore, our risk of incurring liability for a security breach on a customer website would increase if the security breach were to occur following our sale to a customer of an SSL certificate that proved ineffectual in preventing it. Finally, we are exposed to potential liability as a result of our private domain name registration service, wherein we become the domain name registrant, on a proxy basis, on behalf of our customers. While we have a policy of providing the underlying Whois information and reserve the right to cancel privacy services on domain names giving rise to domain name disputes including when we receive reasonable evidence of an actionable harm, the safeguards we have in place may not be sufficient to avoid liability in the future, which could increase our costs of doing business.

***The international nature of our business exposes us to certain business risks that could limit the effectiveness of our growth strategy and cause our results of operations to suffer.***

Expansion into international markets is an element of our growth strategy. Introducing and marketing our services internationally, developing direct and indirect international sales and support channels and managing foreign personnel and operations will require significant management attention and financial resources. We face a number of risks associated with expanding our business internationally that could negatively impact our results of operations, including:

- management, communication and integration problems resulting from cultural differences and geographic dispersion;
- compliance with foreign laws, including laws regarding liability of online resellers for activities of customers and more stringent laws in foreign jurisdictions relating to the privacy and protection of third-party data;
- accreditation and other regulatory requirements to provide domain name registration, website hosting and other services in foreign jurisdictions;
- competition from companies with international operations, including large international competitors and entrenched local companies;
- to the extent we choose to make acquisitions to enable our international expansion efforts, the identification of suitable acquisition targets in the markets into which we want to expand;
- difficulties in protecting intellectual property rights in international jurisdictions;
- political and economic instability in some international markets;
- sufficiency of qualified labor pools in various international markets;
- currency fluctuations and exchange rates;
- potentially adverse tax consequences or an inability to realize tax benefits; and

the lower level of adoption of the Internet in many international markets.

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We may not succeed in our efforts to expand our international presence as a result of the factors described above or other factors that may have an adverse impact on our overall financial condition and results of operations.

***We currently license many third party technologies and may need to license further technologies which could delay and increase the cost of product and service developments***

We currently license certain technologies from third parties and incorporate them into certain of our services including email, anti-spam, anti-virus and web site publishing tools. The Internet services market is evolving and we may need to license additional technologies to remain competitive. We may not be able to license these technologies on commercially reasonable terms or at all. To the extent we cannot license necessary solutions, we may have to devote our resources to development of such technologies, which could delay and increase the cost of product and service developments overall.

In addition, we may fail to successfully integrate licensed technology into our services. These third party licenses may expose us to increased risks, including risks related to the integration of new technology and potential intellectual property infringement claims. In addition, an inability to obtain needed licenses could delay product and service development until equivalent technology can be identified, licensed and integrated. Any delays in services or integration problems could hinder our ability to attract and retain customers and cause our business and operating results to suffer.

***Our advertising revenues may be subject to fluctuations.***

We believe that Internet advertising spending, as in traditional media, fluctuates significantly with economic cycles and during any calendar year, with spending being weighted towards the end of the year to reflect trends in the retail industry. Our advertisers can generally terminate their contracts with us at any time. Advertising spending is particularly sensitive to changes in general economic conditions and typically decreases when economic conditions are not favorable. A decrease in demand for Internet advertising could have a material adverse effect on our business, financial condition and results of operations.

***We may acquire companies or make investments in, or enter into licensing arrangements with, other companies with technologies that are complementary to our business and these acquisitions or arrangements could disrupt our business, cause us to require additional financing and dilute your holdings in our company.***

We may acquire companies, assets or the rights to technologies in the future in order to develop new services or enhance existing services, to enhance our operating infrastructure, to fund expansion, to respond to competitive pressures or to acquire complementary businesses. Entering into these types of arrangements entails many risks, any of which could materially harm our business, including:

the diversion of management's attention from other business concerns;

the failure to effectively integrate the acquired technology or company into our business;

the incurring of significant acquisition costs;

the loss of key employees from either our current business or the acquired business; and

the assumption of significant liabilities of the acquired company.

In addition, absent sufficient cash flows from operations, we may need to engage in equity or debt financings to secure additional funds to meet our operating and capital needs. We may not be able to secure additional debt or equity financing on favorable terms, or at all, at the time when we need that funding. In addition, even though we may have sufficient cash flow, we may still elect to sell additional equity or debt securities or obtain credit facilities for other reasons. If we raise additional funds through further issuances of equity or convertible debt securities, our existing shareholders could suffer



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significant dilution in their percentage ownership of our company, and any new equity securities we issue could have rights, preferences and privileges senior to those of holders of our common stock. Any debt financing secured by us in the future could involve restrictive covenants relating to our capital raising activities and other financial and operational matters, which might make it more difficult for us to obtain additional capital, to pay dividends and to pursue business opportunities, including potential acquisitions. In addition, if we decide to raise funds through debt or convertible debt financings, we may be unable to meet our interest or principal payments.

Any of the foregoing or other factors could harm our ability to achieve anticipated levels of profitability from acquired businesses or to realize other anticipated benefits of acquisitions. We may not be able to identify or consummate any future acquisitions on favorable terms, or at all. If we do effect an acquisition, it is possible that the financial markets or investors will view the acquisition negatively. Even if we successfully complete an acquisition, it could adversely affect our business.

***Our corporate culture has contributed to our success, and if we cannot maintain this culture as we grow, we could lose the innovation, creativity and teamwork fostered by our culture, and our business may be harmed.***

We believe that a critical contributor to our success has been our corporate culture, which we believe fosters innovation, creativity and teamwork. As our organization grows and we are required to implement more complex organizational management structures, we may find it increasingly difficult to maintain the beneficial aspects of our corporate culture. This could negatively impact our future success.

***Our business depends on a strong brand. If we are not able to maintain and enhance our brand, our ability to expand our customer base will be impaired and our business and operating results will be harmed.***

In recognition of the evolving nature of the internet services market and to make it easier to clearly differentiate each service we offer from our competitors, we enhanced our branding by focusing our service offerings under four distinct brands namely "OpenSRS", "YummyNames", "Hover" and "Butterscotch". We also believe that maintaining and enhancing the "Tucows" corporate brand and our service brands is critical to expanding our customer base. We anticipate that, as our market becomes increasingly competitive, maintaining and enhancing our brands may become increasingly difficult and expensive. Maintaining and enhancing our brands will depend largely on our ability to be a technology leader providing high quality products and services, which we may not do successfully. To date, we have engaged in relatively little direct brand promotion activities. This enhances the risk that we may not successfully implement brand enhancement efforts in the future.

***If we fail to protect our proprietary rights, the value of those rights could be diminished.***

We rely upon copyright, trade secret and trademark law, confidentiality and nondisclosure agreements, invention assignment agreements and work-for-hire agreements to protect our proprietary technology, all of which offer only limited protection. We cannot ensure that our efforts to protect our proprietary information will be adequate to protect against infringement and misappropriation by third parties, particularly in foreign countries where laws or law enforcement practices may not protect proprietary rights as fully as in the United States of America and Canada.

We have licensed, and may in the future license, some of our trademarks and other proprietary rights to others. Third parties may also reproduce or use our intellectual property rights without seeking a license and thus benefit from our technology without paying for it. Third parties could also independently develop technology, processes or other intellectual property that are similar to or superior to those used by us. Actions by licensees, misappropriation of the intellectual property rights or independent development by others of similar or superior technology might diminish the value of our proprietary rights or damage our reputation.

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The unauthorized reproduction or other misappropriation of our intellectual property rights, including copying the look, feel and functionality of our website could enable third parties to benefit from our technology without us receiving any compensation. The enforcement of our intellectual property rights may depend on our taking legal action against these infringing parties, and we cannot be sure that these actions will be successful.

Because of the global nature of the Internet, our websites can be viewed worldwide. However, we do not have intellectual property protection in every jurisdiction. Furthermore, effective trademark, service mark, copyright and trade secret protection may not be available in every country in which our services become available over the Internet. In addition, the legal standards relating to the validity, enforceability and scope of protection of intellectual property rights in Internet-related industries are uncertain and still evolving.

***We may not be able to realize the intended and anticipated benefits from our acquisitions of expiring domain names, which could affect the value of these acquisitions to our business and our ability to meet our financial obligations and targets.***

We may not be able to realize the intended and anticipated benefits that we currently expect from our acquisition of expiring domain names. These intended and anticipated benefits include increasing our cash flow from operations, broadening our Internet service offerings and delivering services that strengthen our reseller relationships.

Factors that could affect our ability to achieve these benefits include:

A significant amount of revenue attributed to our domain name assets comes from the provision of personalized email services and the generation of revenue from third party advertisements on parked pages. Some of our existing resellers who provide similar services may perceive this as a competitive threat and therefore may decide to terminate their agreements with us because of our acquisitions of a substantial number of expiring domain names.

We will need to continue to acquire commercially valuable expiring domain names to grow our presence in the field of direct navigation. We will need to continuously improve our technologies to acquire valuable expiring domain names as competition in the marketplace for appropriate expiring domain names intensifies. Our domain name acquisition efforts are subject to rules and guidelines established by registries which maintain Internet domain name registrations and other registrars who process and facilitate Internet domain name registrations. The registries and registrars may change the rules and guidelines for acquiring expiring domains in ways that may prove detrimental to our domain name acquisition efforts.

The business of direct navigation is dependent on current technologies and user practices. If browser or search technologies were to change significantly, the practice of direct navigation may be altered to our disadvantage.

If the acquired assets are not integrated into our business as we anticipate, we may not be able to achieve the benefits of these acquired assets or realize the value paid for the asset acquisitions, which could materially harm our business, financial condition and results of operations.

***We do not control the means by which end users access our web sites and material changes to current navigation practices or technologies or marketing practices could result in a material adverse effect on our business.***

The success of our parked pages business depends in large part upon the current end user tendency to type desired destinations directly into the web browser. End users employ this practice of direct navigation to access our web sites primarily through the following methods: directly accessing our web sites by typing descriptive keywords or keyword strings into the uniform resource locator, or URL,

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address box of an Internet browser, accessing our web sites by clicking on bookmarked web sites and accessing our web sites indirectly through search engines and directories.

Each of these methods requires the use of a third party product or service, such as an Internet browser or search engine or directory. Internet browsers may provide alternatives to the URL address box to locate web sites, and search engines may from time to time change and establish rules regarding the indexing and optimization of web sites. Product developments and market practices for these means of access to our web sites are not within our control. We may experience a decline in traffic to our web sites if third party browser technologies or search engine methodologies and rules, including those affecting marketing efforts, are changed to our disadvantage.

***If the practice of direct navigation becomes less popular either as a result of evolving technologies or user practices, our ability to generate revenue from the practice of click through advertising may suffer.***

A significant amount of revenue generated from the commercialization of domain names owned by the Company is dependent on our agreements with third party providers. The monetization of these domain names is currently largely dependent on the paid listings allocated by these providers to the websites associated with our domain names. This allocation may depend on each provider's advertiser base, internal policies and other factors and determinations that may or may not be controlled by or known to us.

***We may experience unforeseen liabilities in connection with our domain name portfolio, which could negatively impact our financial results.***

We currently own a portfolio of domain names that were previously owned by another third-party. In addition, we are currently acquiring, and intend to continue to acquire, other previously owned domain names. While we have a policy against acquiring domain names that infringe on third-party intellectual property rights, including trademarks or confusingly similar business names, in some cases, these acquired names may have trademark significance that is not readily apparent to us or is not identified by us in the bulk purchasing process. As a result, we may face demands by third party trademark owners asserting infringement or dilution of their rights and seeking transfer of the domain names through the Uniform Domain Name Resolution Policy adopted by ICANN or actions under the ACPA. We may also face actions from third-parties under national trademark or anti-competition legislation.

We review each claim or demand on its merits and we intend to transfer any such previously owned domain names acquired by us to parties that have demonstrated a valid prior right of claim. We cannot, however, guarantee that we will be able to resolve all such disputes without litigation. The potential violation of third party intellectual property rights and potential causes of action under consumer protection laws may subject us to unforeseen liabilities, including injunctions and judgments for monetary damages.

***Once any infringement is detected, disputes concerning the ownership or rights to use intellectual property could be costly and time-consuming to litigate, may distract management from operating the business, and may result in us losing significant rights and our ability to operate all or a portion of our business.***

Claims of infringement of intellectual property or other rights of third parties against us could result in substantial costs. Third parties may assert claims of infringement of patents or other intellectual property rights against us concerning past, current or future technologies. Content obtained from third parties and distributed over the Internet by us may result in liability for defamation, negligence, intellectual property infringement, product or service liability and dissemination of computer viruses or other disruptive problems. We may also be subject to claims from third parties asserting trademark infringement, unfair competition and violation of publicity and privacy rights



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relating specifically to domains. As a domain name registrar, we regularly become involved in disputes over registration of domain names. Most of these disputes arise as a result of a third party registering a domain name that is identical or similar to another party's trademark or the name of a living person. These disputes are typically resolved through the Uniform Domain-Name Dispute-Resolution Policy, or UDRP, ICANN's administrative process for domain name dispute resolution, or less frequently through litigation under the Anticybersquatting Consumer Protection Act, or ACPA, or under general theories of trademark infringement or dilution. The UDRP generally does not impose liability on registrars, and the ACPA provides that registrars may not be held liable for registering or maintaining a domain name absent a showing of bad faith intent to profit or reckless disregard of a court order by the registrars. However, we may face liability if we fail to comply in a timely manner with procedural requirements under these rules. In addition, these processes typically require at least limited involvement by us, and therefore increase our cost of doing business. The volume of domain name registration disputes may increase in the future as the overall number of registered domain names increases.

These claims and any related litigation could result in significant costs of defense, liability for damages and diversion of management's time and attention. Any claims from third parties may also result in limitations on our ability to use the intellectual property subject to these claims unless we are able to enter into agreements with the third parties making these claims. If a successful claim of infringement is brought against us and we fail to develop non-infringing technology or to license the infringed or similar technology on a timely basis, we may have to limit or discontinue the business operations which used the infringing technology.

We rely on technologies licensed from other parties. These third-party technology licenses may infringe on the proprietary rights of others and may not continue to be available on commercially reasonable terms, if at all. The loss of this technology could require us to obtain substitute technology of lower quality or performance standards or at greater cost, which could increase our costs and make our products and services less attractive to customers.

***The law relating to the liability of online services companies for data and content carried on or disseminated through their networks is currently unsettled and could expose us to unforeseen liabilities.***

It is possible that claims could be made against online services companies under U.S., Canadian or foreign law for defamation, negligence, copyright or trademark infringement, or other theories based on data or content disseminated through their networks, even if a user independently originated this data or content. Several private lawsuits seeking to impose liability upon Internet service companies have been filed in U.S. and foreign courts. While the United States has passed laws protecting ISPs from liability for actions by independent users in limited circumstances, this protection may not apply in any particular case at issue. Our ability to monitor, censor or otherwise restrict the types of data or content distributed through our network is limited. Failure to comply with any applicable laws or regulations in particular jurisdictions could result in fines, penalties or the suspension or termination of our services in these jurisdictions. Our insurance may not be adequate to compensate or may not cover us at all in the event we incur liability for damages due to data and content carried on or disseminated through our network. Any costs not covered by insurance that are incurred as a result of this liability or alleged liability, including any damages awarded and costs of litigation, could harm our business and prospects.

***Privacy concerns relating to our technology could damage our reputation and deter current and potential users from using our services.***

From time to time, concerns have been expressed about whether our services compromise the privacy of our users and others. Concerns about our practices with regard to the collection, use, disclosure or security of personal information or other privacy-related matters, even if unfounded, could damage our reputation and operating results and expose us to litigation and possible liability, including claims for unauthorized purchases with credit card information, impersonation, or fraud claims and

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other claims relating to the misuse of personal information and unauthorized marketing purposes. While we strive to comply with all applicable data protection laws and regulations, as well as our own privacy policies, any failure or perceived failure to comply may result in proceedings or actions against us by government entities or others, which could potentially have an adverse effect on our business.

In addition, due to the fact that our services are web based, the amount of data we store for our users on our servers (including personal information) has been increasing. Any systems failure or compromise of our security that results in the release of our users' data could seriously limit the adoption of our services as well as harm our reputation and brand and, therefore, our business. We may also need to expend significant resources to protect against security breaches. The risk that these types of events could seriously harm our business is likely to increase as we expand the number of Internet services we offer.

A large number of legislative proposals pending before the United States Congress, various state legislative bodies and foreign governments concern data protection. In addition, the interpretation and application of data protection laws in Europe and elsewhere are still unsettled. We cannot guarantee that our current information-collection procedures and disclosure policies will be found to be in compliance with existing or future laws or regulations. If our policies and procedures are found not to be in compliance, in addition to the possibility of fines, this could result in an order requiring that we change our data practices, which could in turn have a material effect on our business. Complying with these various laws could cause us to incur substantial costs or require us to change our business practices in a manner adverse to our business.

***Because we are required to recognize revenue for our services over the term of the applicable customer agreement, changes in our sales may not be immediately reflected in our operating results.***

We recognize revenue from our customers ratably over the respective terms of their agreements with us as required by GAAP. Typically, our domain name registration agreements have terms that range from one to ten years, and our website hosting agreements have annual or month-to-month terms. Accordingly, any increases or decreases in sales during a particular period do not translate into immediate, proportional increases or decreases in revenue during that period, and a substantial portion of the revenue that we recognize during a quarter is derived from deferred revenue from customer agreements that we entered into during previous quarters. As a result, we may not generate net earnings despite substantial sales activity during a particular period, since we are not permitted under GAAP to recognize all of the revenue from these sales immediately, and because we are required to reflect a significant portion of our related operating expenses in full during that period. Conversely, the existence of substantial deferred revenue may prevent deteriorating sales activity from becoming immediately observable in our consolidated statement of operations.

In addition, we may not be able to adjust spending in a timely manner to compensate for any unexpected revenue shortfall, and any significant shortfall in revenue relative to planned expenditures could negatively impact our business and results of operations.

***Currency fluctuations may adversely affect us.***

Our revenue is primarily realized in U.S. dollars and a major portion of our operating expenses are paid in Canadian dollars. Fluctuations in the exchange rate between the U.S. dollar and the Canadian dollar may have a material effect on our business, financial condition and results from operations. In particular, we may be adversely affected by a significant weakening of the U.S. dollar against the Canadian dollar on a quarterly and an annual basis. Our policy with respect to foreign currency exposure is to manage our financial exposure to certain foreign exchange fluctuations with the objective of neutralizing some or all of the impact of foreign currency exchange movements by entering into foreign exchange forward contracts to mitigate the exchange risk on a portion of our Canadian

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dollar exposure. We may not always enter into such forward contracts and such contracts may not always be available and economical for us. Additionally, the forward rates established by the contracts may be less advantageous than the market rate upon settlement. We do not account for these instruments as hedges in our consolidated financial statements.

***If we do not maintain a low rate of credit card chargebacks, we will face the prospect of financial penalties and could lose our ability to accept credit card payments from customers, which would have a material adverse effect on our business, financial condition and results of operations.***

A substantial majority of our revenue originates from online credit card transactions. Under current credit card industry practices, we are liable for fraudulent and disputed credit card transactions because we do not obtain the cardholder's signature at the time of the transaction, even though the financial institution issuing the credit card may have authorized the transaction. Under credit card association rules, penalties may be imposed at the discretion of the association. Any such potential penalties would be imposed on our credit card processor by the association. Under our contract with our processor, we are required to reimburse our processor for such penalties. Our current level of fraud protection, based on our fraudulent and disputed credit card transaction history, is within the guidelines established by the credit card associations. However, we face the risk that one or more credit card associations may, at any time, assess penalties against us or terminate our ability to accept credit card payments from customers, which would have a material adverse effect on our business, financial condition and results of operations.

***Forecasting our tax rate is complex and subject to uncertainty.***

We are subject to income and other taxes in a number of jurisdictions and our tax structure is subject to review by both domestic and foreign tax authorities. We must make significant assumptions, judgments and estimates to determine our current provision for income taxes, deferred tax assets and liabilities and any valuation allowance that may be recorded against our deferred tax assets. Although we believe that our estimates are reasonable, the ultimate determination of our tax liability is always subject to review by the applicable tax authorities. Any adverse outcome of such a review could have a negative effect on our operating results and financial condition in the period or periods for which such determination is made. Our current and future tax liabilities could be adversely affected by:

international income tax authorities, including the Canada Revenue Agency and the U.S. Internal Revenue Service, challenging the validity of our arm's-length related party transfer pricing policies or the validity of our contemporaneous documentation.

changes in the valuation of our deferred tax assets; or

changes in tax laws, regulations, accounting principles or the interpretations of such laws.

***In the event we are unable to satisfy regulatory requirements relating to internal control over financial reporting, or if these internal controls are not effective, our business and financial results may suffer.***

Enacted in July 2010, The Dodd-Frank Act amended the Sarbanes-Oxley Act to smaller reporting companies, like Tucows, from the requirement to obtain an audit report on internal controls over financial reporting.

Effective internal controls are necessary for us to provide reasonable assurance with respect to our financial reports and to effectively prevent fraud. If we cannot provide reasonable assurance with respect to our financial reports and effectively prevent fraud, our brand and operating results could be harmed. Pursuant to the Sarbanes-Oxley Act of 2002, we are required to furnish a report by management on internal control over financial reporting, including management's assessment of the effectiveness of such control. Internal control over financial reporting may not prevent or detect

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misstatements because of its inherent limitations, including the possibility of human error, the circumvention or overriding of controls, or fraud. Therefore, even effective internal controls cannot guarantee assurance with respect to the preparation and fair presentation of financial statements. In addition, projections of any evaluation of the effectiveness of internal control over financial reporting to future periods are subject to the risk that the control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. If we fail to maintain the adequacy of our internal controls, including any failure to implement required new or improved controls, or if we experience difficulties in their implementation, our business and operating results could be harmed, we could fail to meet our reporting obligations, which could have a material adverse effect on our operating results and on our stock price, and it could make it more difficult for us to attract and retain qualified persons to serve on our Board of Directors or as executive officers.

***Impairment of goodwill and other intangible assets would result in a decrease in earnings.***

Current accounting rules require that goodwill and other intangible assets with indefinite useful lives may no longer be amortized, but instead must be tested for impairment at least annually. These rules also require that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. To the extent such evaluation indicates that the useful lives of intangible assets are different than originally estimated, the amortization period is reduced or extended and, accordingly, the quarterly amortization expense is increased or decreased. We have substantial goodwill and other intangible assets, and we would be required to record a significant charge to earnings in our financial statements during the period in which any impairment of our goodwill or amortizable intangible assets is determined. Any impairment charges or changes to the estimated amortization periods could have a material adverse effect on our financial results.

***We could suffer uninsured losses.***

Although we maintain general liability insurance, claims could exceed the coverage obtained or might not be covered by our insurance. While we typically obtain representations from our technology and content providers and contractual partners concerning the ownership of licensed technology and informational content and obtain indemnification to cover any breach of these representations, we still may not receive accurate representations or adequate compensation for any breach of these representations. We may have to pay a substantial amount of money for claims that are not covered by insurance or indemnification or for claims where the existing scope or adequacy of insurance or indemnification is disputed or insufficient.

***A further decline in economic conditions or prolongment of the current economic recession could have a material adverse impact on our business, financial condition and results of operations.***

The national and global economic downturn has resulted in a decline in overall consumer and corporate spending, declines in consumer and corporate access to credit, fluctuations in foreign exchange rates, declines in the value of assets and increased liquidity risks, all of which could materially and negatively impact our business, financial condition and results of operations for the foreseeable future, particularly if the economy continues to decline or the current economic recession is prolonged. Consumer spending patterns are difficult to predict and are sensitive to the general economic climate, the consumers' level of disposable income, consumer debt and overall consumer confidence. Our services may be considered discretionary on the part of many of our current and potential customers and be dependent upon levels of consumer spending. As a result, resellers and consumers considering whether to purchase our services may be influenced by macroeconomic factors that affect consumer spending such as unemployment, continuing increases in fuel costs, conditions in the residential real estate and mortgage markets and access to credit.

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To the extent conditions in the economy remain uncertain or continue to deteriorate, our business could be impacted as customers choose to leave our services, to reduce their service level or to stop purchasing our services. In addition, our efforts to attract new customers may be adversely affected. Declines in consumer spending may also negatively impact our business customers, who may experience decreases in demand for our services. The current economic conditions may also adversely impact our key vendors. In an extended economic recession, decreased consumer spending is likely to result, in a variety of negative effects such as reduction in revenues, increased costs, lower gross margin percentages, increased allowances for doubtful accounts and write-offs of accounts receivable, and recognition of impairments of assets, including goodwill and other intangible assets. Uncertainty and adverse economic conditions may also lead to a decreased ability to collect payment for our services due primarily to a decline in the ability of our business customers to use or access credit, including through credit cards, which is how most of our customers pay for our services. We also expect to continue to experience volatility in foreign exchange rates, which could negatively impact the amount of expenses we incur and the net assets we record in future periods. If any of the above risks are realized, we may experience a material adverse effect on our business, financial condition and results of operations.

***Our quarterly and annual operating results may fluctuate and our future revenues and profitability are uncertain.***

Our quarterly and annual operating results may fluctuate significantly in the future as a result of a variety of factors, many of which are outside of our control. Our quarterly and annual operating results may be adversely affected by a wide variety of factors, including:

our ability to maintain revenue growth at current levels or anticipate a decline in revenue from any of our services;

our ability to identify and develop new technologies or services and to commercialize those technologies into new services in a timely manner;

the mix of our services sold during the quarter or year;

our ability to make appropriate decisions which will position us to achieve further growth;

concentrated capital expenditures in any particular period to support our growth or for other reasons;

changes in our pricing policies or those of our competitors, changes in domain name fees charged to us by Internet registries or ICANN, or other competitive pressures on selling prices;

our ability to identify, hire, train, motivate and retain highly qualified personnel, and to achieve targeted productivity levels;

market acceptance of Internet services generally and of new and enhanced versions of our services in particular;

our ability to establish and maintain a competitive advantage;

the continued development of our global distribution channel and our ability to compete in multiple countries successfully as part of our sales and marketing strategy;

the number and significance of service enhancements and new service and technology announcements by our competitors;

our ability to identify, develop, deliver, and introduce in a timely manner new and enhanced versions of our current service offerings that anticipate market demand and address customer needs;



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changes in foreign currency exchange rates and issues relating to the conversion to the Canadian dollar;

foreign, federal or state regulation affecting our business;

our ability to continue to attract users to our website;

our ability to attract software developers to participate in our Author Resource Center;

our ability to continue to attract advertisers to place content on our website;

technical difficulties or other factors that result in system downtime;

seasonality of the markets and businesses of our customers;

news relating to our industry as a whole;

our ability to enforce our intellectual property rights; and

our ability to manage Internet fraud and information theft.

Our operating expenses may increase. We base our operating expense budgets on expected revenue trends that are more difficult to predict in periods of economic uncertainty. We intend to continue our efforts to control discretionary spending; however, we will continue to selectively incur expenditures in areas that we believe will strengthen our position in the marketplace. If we do not meet revenue goals, we may not be able to meet reduced operating expense levels and our operating results will suffer. It is possible that in one or more future quarters, our operating results may be below our expectations and the expectations of public market analysts and investors. In that event, the price of our common stock may fall.

**Risks Related To the Internet and Our Technology**

*Our business could be materially harmed if the administration and operation of the Internet no longer rely upon the existing domain system.*

The domain registration industry continues to develop and adapt to changing technology. This development may include changes in the administration or operation of the Internet, including the creation and institution of alternate systems for directing Internet traffic without the use of the existing domain system. Some of our competitors have begun registering domains with extensions that rely on such alternate systems. These competitors are not subject to ICANN accreditation requirements and restrictions. Other competitors have attempted to introduce naming systems that use keywords rather than traditional domains. The widespread acceptance of any alternative systems could eliminate the need to register a domain to establish an online presence and could materially adversely affect our business, financial condition and results of operations.

*The law relating to the use of and ownership in intellectual property on the Internet is currently unsettled and may expose us to unforeseen liabilities.*

There have been ongoing legislative developments and judicial decisions concerning trademark infringement claims, unfair competition claims and dispute resolution policies relating to the registration of domains. To help protect ourselves from liability in the face of these ongoing legal developments, we have taken the following precautions:

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Our standard registration agreement requires that each registrant indemnify, defend and hold us harmless for any dispute arising from the registration or use of a domain registered in that person's name; and



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Since December 1, 1999, we have required our resellers to ensure that all registrants are bound to the Uniform Domain Name Dispute Resolution Policy as approved by ICANN.

Despite these precautions, we cannot be assured that our indemnity and dispute resolution policies will be sufficient to protect us against claims asserted by various third parties, including claims of trademark infringement and unfair competition.

New laws or regulations concerning domains and registrars may be adopted at any time. Our responses to uncertainty in the industry or new regulations could increase our costs or prevent us from delivering our domain registration services over the Internet, which could delay growth in demand for our services and limit the growth of our revenues. New and existing laws may cover issues such as:

pricing controls;

the creation of additional generic top level domains and country code domains;

consumer protection;

cross-border domain registrations;

trademark, copyright and patent infringement;

domain dispute resolution; and

the nature or content of domains and domain registration.

An example of legislation passed in response to novel intellectual property concerns created by the Internet is the ACPA enacted by the United States government in November 1999. This law seeks to curtail a practice commonly known in the domain registration industry as cybersquatting. A cybersquatter is generally defined in the ACPA as one who registers a domain that is identical or similar to another party's trademark, or the name of another living person, with the bad faith intent to profit from use of the domain. The ACPA states that registrars may not be held liable for registration or maintenance of a domain for another person absent a showing of the registrar's bad faith intent to profit from the use of the domain. Registrars may be held liable, however, if they do not comply promptly with procedural provisions of the ACPA. For example, if there is litigation involving a domain, the registrar is required to deposit a certificate representing the domain registration with the court. If we are held liable under the ACPA, any liability could have a material adverse effect on our business, financial condition and results of operations.

***If Internet usage does not grow or if the Internet does not continue to expand as a medium for commerce, our business may suffer.***

Our success depends upon the continued development and acceptance of the Internet as a widely used medium for commerce and communication. Rapid growth in the uses of, and interest in, the Internet is a relatively recent phenomenon and its continued growth cannot be assured. A number of factors could prevent continued growth, development and acceptance, including:

the unwillingness of companies and consumers to shift their purchasing from traditional vendors to online vendors;

the Internet infrastructure may not be able to support the demands placed on it, and its performance and reliability may decline as usage grows;

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security and authentication issues may create concerns with respect to the transmission over the Internet of confidential information; and

privacy concerns, including those related to the ability of websites to gather user information without the user's knowledge or consent, may impact consumers' willingness to interact online.

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Any of these issues could slow the growth of the Internet, which could limit our growth and revenues.

***We believe that part of our growth will be derived from resellers in international markets and may suffer if Internet usage does not continue to grow globally.***

We believe that a major source of growth for Internet-based companies will come from individuals and businesses outside the United States where Internet access and use is currently less prevalent. A substantial number of our resellers are currently based outside the United States and we plan to grow our business in other countries. If Internet usage in these jurisdictions does not increase as anticipated, our revenues may not grow as anticipated.

***We may be unable to respond to the rapid technological changes in the industry, and our attempts to respond may require significant capital expenditures.***

The Internet and electronic commerce are characterized by rapid technological change. Sudden changes in user and customer requirements and preferences, the frequent introduction of new applications and services embodying new technologies and the emergence of new industry standards and practices could make our applications, services and systems obsolete. The emerging nature of applications and services in the Internet application and services industry and their rapid evolution will require that we continually improve the performance, features and reliability of our applications and services. Our success will depend, in part, on our ability:

to develop and license new applications, services and technologies that address the increasingly sophisticated and varied needs of our current and prospective customers; and

to respond to technological advances and emerging industry standards and practices on a cost-effective and timely basis.

The development of applications and services and other proprietary technology involves significant technological and business risks and requires substantial expenditures and lead-time. We may be unable to use new technologies effectively or adapt our internally developed technology and transaction- processing systems to customer requirements or emerging industry standards in a timely manner, or at all. Our internal development teams may also be unable to keep pace with new technological developments that affect the marketplace for our services. In addition, as we offer new services and functionality, we will need to ensure that any new services and functionality are well integrated with our current services, particularly as we offer an increasing number of our services as part of bundled suites. To the extent that any new services offered by us do not interoperate well with our existing services, our ability to market and sell those new services would be adversely affected and our revenue level and ability to achieve and sustain profitability might be harmed. Updating technology internally and licensing new technology from third parties may require us to incur significant additional capital expenditures.

***We could experience system failures and capacity constraints which could diminish our ability to effectively provide our services and could damage our reputation and harm our operating results.***

The availability of our services depends on the continuing operation of our information technology and communications systems. Any damage to or failure of our systems could result in interruptions in our service, which could reduce our revenues and profits, and damage our brand. Our systems are vulnerable to damage or interruption from earthquakes, terrorist attacks, floods, fires, power loss, telecommunications failures, computer viruses, computer denial of service attacks or other attempts to harm our systems. Some of our data centers are located in areas with a high risk of major earthquakes. Our data centers are also subject to break-ins, sabotage and intentional acts of vandalism, and to potential disruptions if the operators of these facilities have financial difficulties. Some of our systems

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are not fully redundant, and our disaster recovery planning cannot account for all eventualities. The occurrence of a natural disaster, a decision to close a facility without adequate notice or other unanticipated problems at our data centers could result in lengthy interruptions in our service.

***Our systems face security risks, and any compromise of the security of these systems could result in liability for damages and in lost customers.***

Our security systems may be vulnerable to unauthorized access by hackers or others, computer viruses and other disruptive problems. Someone who is able to circumvent security measures could misappropriate customer or proprietary information or cause interruptions in Internet operations. Internet and online resellers have in the past experienced, and may in the future experience, interruptions in service because of the accidental or intentional actions of Internet users, current and former employees or others.

We may need to expend significant capital and other resources to protect against the threat of security breaches or alleviate problems caused by breaches. Unauthorized persons may be able to circumvent the measures that are implemented in the future. Eliminating computer viruses and alleviating other security problems may require interruptions, delays or cessation of service to users accessing our websites and the web pages that deliver our content services. Repeated or substantial interruptions could result in the loss of customers and reduced revenues.

***We may have difficulty scaling and adapting our existing architecture to accommodate increased traffic and technology advances or changing business requirements, which could lead to the loss of customers and cause us to incur additional expenses.***

To be successful, our network infrastructure must perform well and be reliable. The greater the user traffic and the greater the complexity of our services, the more computing power we will need. We have spent and expect to continue to spend substantial amounts on the purchase of new equipment to upgrade our technology and network infrastructure to enable it to handle increased traffic. This expansion is expensive and complex and could result in inefficiencies or operational failures. If we do not expand successfully, or if we experience inefficiencies and operational failures, the quality of our services and our customers' experience could decline. This could damage our reputation and lead us to lose current and potential customers. Cost increases, loss of traffic or failure to accommodate new technologies or changing business requirements could harm our operating results and financial condition.

***We rely on bandwidth providers, data centers and other vendors in providing services to our customers, and any failure or interruption in the services provided by these third parties could harm our ability to operate our business and damage our reputation.***

We rely on vendors, including data center and bandwidth providers in providing services to our customers. Any disruption in the network access or co-location services provided by these providers or any failure of these providers to handle current or increased volumes of use could significantly harm our business. Any financial or other difficulties our providers face may also have negative effects on our business. We exercise little control over these vendors, which increases our vulnerability to problems with the services they provide. We license technology and related databases to facilitate certain aspects of our data center and connectivity operations, including Internet traffic management services. We have experienced and expect to continue to experience interruptions and delays in service and availability for such elements. Any errors, failures, interruptions or delays in connection with these technologies and information services could harm our relationship with customers, adversely affect our brand and expose us to liabilities.

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***Lack of consumer confidence in the security of on-line financial transactions could negatively impact our business.***

Consumers may not adopt online services if they are not confident that financial transactions over the Internet can be undertaken securely and confidentially. Although there is security technology currently available for online transactions, many Internet users may not use the Internet for commercial transactions because of security concerns. These concerns may be heightened by well-publicized security breaches of any Internet-related service, which could deter consumers from using our services provided by our solution. If consumers do not have confidence in the security for online services transactions that the current technologies provide, our revenue will not increase and may decrease.

***We may be accused of intellectual property infringement of the technology we have employed to support both our back end platform and the products and services we offer to and through our resellers and may be sued for damages caused by actual use of the platforms or products and services and we may be required to pay substantial damage awards.***

We seek to ensure that we have licensed or otherwise secured the necessary rights to use and offer for use all intellectual property relating to our platforms and the services we offer resellers through the platforms. Despite our efforts, we may be sued by third parties claiming rights in and to the technology we employ or by third parties who claim to have suffered as a result of any use, or inability to use, the platforms, products and services. If we are sued, defense of any such claims may require the resources of both our time and money. If a third-party is successful in its assertions, we may be required to pay damages that may have a material impact on our financial resources.

**Governmental and Regulatory Risks**

***Governmental and regulatory policies or claims concerning the domain registration system, and industry reactions to those policies or claims, may cause instability in the industry and disrupt our domain registration business.***

**ICANN Oversight of Domain Name Registration System**

Before 1999, Network Solutions managed the domain registration system for the .com, .net and .org domains on an exclusive basis under a cooperative agreement with the U.S. government. In November 1998, the U.S. Department of Commerce authorized ICANN, a private sector, not for profit corporation, to oversee key aspects of the domain registration system. ICANN has been subject to strict scrutiny by the public and by the government in the United States of America. For example, in the United States of America, Congress has held hearings to evaluate ICANN's selection process for new top level domains. In addition, ICANN faces significant questions regarding its financial viability and efficacy as a private sector entity. ICANN may continue to evolve both its long term structure and mission to address perceived shortcomings such as a lack of accountability to the public and a failure to maintain a diverse representation of interests on its Board of Directors. We continue to face the risks that:

the U.S. or any other government may reassess its decision to introduce competition into, or ICANN's role in overseeing, the domain registration market;

the Internet community or the U.S. Department of Commerce or U.S. Congress may refuse to recognize ICANN's authority or support its policies, which could create instability in the domain registration system;

some of ICANN's policies and practices, and the policies and practices adopted by registries and registrars, could be found to conflict with the laws of one or more jurisdictions;

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ICANN may lose any one of the several claims pending against it in both the U.S. and international courts, in which case its credibility may suffer and its policies may be discredited;

the terms of the Registrar Accreditation Agreement, under which we are accredited as a registrar, could change in ways that are disadvantageous to us or under certain circumstances could be terminated by ICANN preventing us from operating our Registrar;

ICANN and, under their registry agreements, VeriSign and other registries may impose increased fees received for each ICANN accredited registrar and/or domain name registration managed by those registries;

ICANN or any registries may implement policy changes that would impact our ability to run our current business practices throughout the various stages of the lifecycle of a domain name;

foreign constituents may succeed in their efforts to have domain name registration removed from a U.S. based entity and placed in the hands of an international cooperative; and

international regulatory or governing bodies, such as the International Telecommunications Union or the European Union, may gain increased influence over the management and regulation of the domain registration system, leading to increased regulation in areas such as taxation and privacy.

If any of these events occur, they could create instability in the domain registration system. These events could also disrupt or suspend portions of our domain registration solution, which would result in reduced revenue.

***Governmental Regulation Affecting the Internet***

To date, government regulations have not materially restricted use of the Internet in most parts of the world. The legal and regulatory environment pertaining to the Internet, however, is uncertain and may change. New laws may be passed, existing but previously inapplicable laws may be deemed to apply to the Internet, or existing legal safe harbors may be narrowed, both by U.S. federal or state governments and by governments of foreign jurisdictions. These changes could affect:

the liability of online resellers for actions by customers, including fraud, illegal content, spam, phishing, libel and defamation, infringement of third-party intellectual property and other abusive conduct;

other claims based on the nature and content of Internet materials, such as pornography;

user privacy and security issues;

consumer protection;

sales and other taxes, including the value-added tax of the European Union member states;

characteristics and quality of services; and

cross-border commerce.

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The adoption of any new laws or regulations, or the application or interpretation of existing laws or regulations to the Internet, could hinder growth in use of the Internet and online services generally, and decrease acceptance of the Internet and online services as a means of communications, commerce and advertising. In addition, such changes in laws could increase our costs of doing business, subject our business to increased liability or prevent us from delivering our services over the Internet, thereby harming our business and results of operations.

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*We may be subject to government regulation that may be costly and may interfere with our ability to conduct business.*

Although transmission of our websites primarily originates in Canada and the United States, the Internet is global in nature. Governments of foreign countries might try to regulate our transmissions or prosecute us for violations of their laws. Because of the increasing popularity and use of the Internet, federal, state and foreign governments may adopt laws or regulations in the future concerning commercial online services and the Internet, with respect to:

user privacy;

children;

copyrights and other intellectual property rights and infringement;

domains;

pricing;

content regulation;

defamation;

taxation; and

the characteristics and quality of products and services.

Laws and regulations directly applicable to online commerce or Internet communications are becoming more prevalent. Laws and regulations such as those listed above or others, if enacted, could expose us to substantial liability and increase our costs of compliance and doing business.

**Risks Related to our Stock**

*We do not intend to declare dividends on our common stock in the immediate future.*

We anticipate that in the immediate future, our earnings, if any, will be retained for use in the business and that no cash dividends will be paid on our common stock. While we may decide to declare such dividends in the future, declaration of dividends on our common stock will depend upon, among other things, future earnings, our operating and financial condition, our capital requirements, ongoing market conditions and general business conditions.

*We are controlled by a limited number of principal shareholders, which may limit your ability to influence corporate matters.*

As of March 17, 2011, three of our principal shareholders beneficially own approximately 33% of the shares of our common stock. These shareholders could control the outcome of any corporate transaction or other matter submitted to our shareholders for approval, including mergers, consolidations and the sale of all or substantially all of our assets, and also could prevent or cause a change in control. The interests of these shareholders may conflict with the interests of our other shareholders.

Third parties may be discouraged from making a tender offer or bid to acquire us because of this concentration of ownership.





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***Our share price is volatile, which may make it difficult for shareholders to sell their shares of common stock when they want to, at an attractive price.***

Our share price has varied recently and the price of our common stock may decrease in the future, regardless of our operating performance. Investors may be unable to resell their common stock following periods of volatility because of the market's adverse reaction to this volatility.

The following factors may contribute to this volatility:

actual or anticipated variations in our quarterly operating results;

interruptions in our services;

seasonality of the markets and businesses of our customers;

announcements of new technologies or new services by our company or our competitors;

our ability to accurately select appropriate business models and strategies;

the operating and stock price performance of other companies that investors may view as comparable to us;

news relating to our industry as a whole; and

news relating to trends in our markets.

The stock market in general, and the market for Internet-related companies in particular, including our company, has experienced volatility. This volatility often has been unrelated to the operating performance of these companies. These broad market and industry fluctuations may cause the price of our common stock to drop, regardless of our performance.

***Future sales of shares of our common stock by our existing shareholders could cause our share price to fall.***

If our shareholders sell substantial amounts of common stock in the public market, the market price of the common stock could fall. The perception among investors that these sales will occur could also produce this effect.

## **ITEM 2. PROPERTIES**

We do not own any real property. Our principal administrative, engineering, marketing and sales office totals approximately 26,937 square feet and is located in Toronto, Ontario under a lease that expires on December 31, 2020. In addition, we also maintain a video studio of approximately 1,640 square feet in Toronto, Ontario and offices of approximately 4,000 square feet in Starkville, Mississippi and approximately 500 square feet in London, United Kingdom.

Substantially all of our computer and communications hardware is located at our facilities or at server hosting facilities in Toronto, Ontario; Ashburn, Virginia and London, United Kingdom.

## **ITEM 3. LEGAL PROCEEDINGS**

We are involved in various investigations, claims and lawsuits arising in the normal conduct of our business, none of which, in our opinion, will materially harm our business. We cannot assure that we will prevail in any litigation. Regardless of the outcome, any litigation may require

us to incur significant litigation expense and may result in significant diversion of management attention.

**ITEM 4. REMOVED AND RESERVED**

Table of Contents**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****Price Range of Common stock**

Our common stock trades on the NYSE Amex under the symbol "TCX" and on the Toronto Stock Exchange under the symbol "TC". The following table sets forth the range of high and low sales prices for our common stock for the periods indicated.

| <b>Year</b> | <b>Fiscal Quarter Ended</b>            | <b>High</b> | <b>Low</b> |
|-------------|--|-------------|------------|
| <b>2011</b> | January 1, 2011 through March 17, 2011 | 0.88        | 0.72       |
| <b>2010</b> | March 31, 2010                         | 0.93        | 0.66       |
|             | June 30, 2010                          | 0.78        | 0.62       |
|             | September 30, 2010                     | 0.69        | 0.58       |
|             | December 31, 2010                      | 0.80        | 0.66       |
| <b>2009</b> | March 31, 2009                         | 0.39        | 0.28       |
|             | June 30, 2009                          | 0.47        | 0.32       |
|             | September 30, 2009                     | 0.61        | 0.36       |
|             | December 31, 2009                      | 0.69        | 0.52       |

Our common stock was listed on the OTC Bulletin Board maintained by NASDAQ under the symbol "TCOW" through August 17, 2005. Our common stock began trading on the NYSE Amex (formerly the American Stock Exchange) on August 18, 2005.

As of March 17, 2011, Tucows had 357 shareholders of record, excluding shareholders whose shares are held in nominee or "street" name by brokers.

We have not declared or paid any cash dividends on our common stock during the fiscal years ended December 31, 2010 and December 31, 2009, and we do not intend to do so in the immediate future, but we may decide to do so in the future depending on ongoing market conditions. Our ability to pay any cash dividends on our common stock, should our Board of Directors decide to do so, is also dependant on our earnings and cash requirements.

Table of Contents**Equity Compensation Plan Information**

On October 8, 2010, the 2006 Equity Compensation Plan was amended to increase the number of shares which have been set aside for issuance by an additional 1.9 million shares to 6.9 million shares

| <b>Plan category</b>                                       | <b>Number of securities to be issued upon exercise of outstanding options, warrants and rights (#)</b> | <b>Weighted average exercise price of outstanding options, warrants and rights (\$)</b> | <b>Number of securities remaining available for future issuance under the plan (excluding securities reflected in the first column) (#)</b> |
|--|--|---|---|
| Equity compensation plans approved by security holders:    |  |   |   |
| 2006 Equity Compensation Plan                              | 4,110,000  | \$ 0.69   | 2,778,700   |
| 1996 Equity Compensation Plan                              | 4,162,249  | \$ 0.42   |   |
| Equity compensation plans not approved by security holders |  |   |   |
| <b>Total</b>   | <b>8,272,249</b>   | <b>\$ 0.56</b>  | <b>2,778,700</b>  |

**Purchases of equity securities by the issuer and affiliated purchasers**

On October 20, 2010, we announced that we successfully concluded a modified Dutch auction tender offer. Under the terms of this offer, we repurchased an aggregate of 3,913,570 shares of our common stock at a purchase price of \$0.70 per share, for a total of \$2,739,499, excluding transaction costs of \$52,802. The purchase price and all transaction costs were funded from available cash. All shares purchased in the tender offer received the same price and all shares repurchased were immediately retired. During the first quarter of Fiscal 2010, we successfully concluded a modified Dutch auction tender offer under which we repurchased an additional 6,341,470 shares of our common stock for a total cost of \$4,439,029, excluding transaction costs of \$51,957.

In addition, on February 24, 2010 we renewed our normal course issuer bid ("NCIB"). The NCIB authorized the repurchase up to 3,854,000 shares of our common stock. During Fiscal 2010 we repurchased 3,409,300 of our common shares under the NCIB at an average purchase price of \$0.71 per share, for a total of \$2,418,471, excluding transaction costs of approximately \$10,000. The purchase price and all transaction costs were funded from available cash. All shares repurchased under the NCIB were immediately retired. This NCIB was terminated upon the commencement of the modified Dutch auction tender offer on September 9, 2010.

Table of Contents**Issuer purchases of equity securities**

The following table provides information about the purchase of equity securities that we made during the fourth quarter of the year ended December 31, 2010 pursuant to our modified Dutch auction tender offer described above:

| Period                | (a)<br>Total number<br>of shares<br>purchased | (b)<br>Average price<br>paid per share(1) | (c)<br>Total<br>number<br>of shares<br>purchased as<br>part of<br>publicly<br>announced<br>plans or<br>programs(2) | (d)<br>Maximum<br>number of<br>shares that<br>may yet be<br>purchased<br>under the plans<br>or programs |
|-----------------------|---|---|--|---|
| October 1 - 31, 2010  | 3,913,570                                     | \$ 0.70                                   | 3,913,570  |   |
| November 1 - 30, 2010 |   |   |  |   |
| December 1 - 31, 2010 |   |   |  |   |
| <b>Total</b>          | 3,913,570                                     | \$ 0.70                                   | 3,913,570  |   |

(1) Average price paid per share as set forth in the table is exclusive of all fees, which amounted to approximately \$0.70 per share.

(2) All shares of common stock listed in the table were repurchased pursuant to a modified Dutch auction tender offer, authorized by our board of directors on August 10, 2010.

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

The following discussion and analysis should be read together with our audited consolidated financial statements for the years ended December 31, 2010, 2009 and 2008 and accompanying notes set forth elsewhere in this report. All financial information is presented in U.S. dollars.

Some of the statements set forth in this section are forward-looking statements relating to our future results of operations. Our actual results may vary from the results anticipated by these statements. Please see "Information Concerning Forward-Looking Statements" on page 1.

**OVERVIEW**

Our mission is to provide simple useful services that help people unlock the power of the Internet. We accomplish this by reducing the complexity our customers' experience as they acquire, deliver or use Internet services such as domain name registration, email and other Internet services.

Our primary distribution channel is a global network of more than 11,000 resellers in more than 100 countries who typically provide their customers, the end-users of the Internet, with a critical component for establishing and maintaining an online presence. Our primary focus is serving the needs of this network of resellers by providing superior services, easy-to-use interfaces, proactive and attentive customer service, reseller-oriented technology and agile design and development processes. We seek to provide superior customer service to our resellers by anticipating their business needs and technical requirements. This includes providing easy-to-use interfaces that enable resellers to quickly and easily integrate our services into their individual business processes, and offering brandable end-user interfaces that emphasize simplicity and visual appeal. We also provide "second tier" support to our resellers by email and phone in the event resellers experience issues or problems with our services. In



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addition, our Network Operating Center provides proactive support to our resellers by monitoring all services and network infrastructure to address deficiencies before customer services are impacted.

We believe that the underlying platforms for our services are one of the most mature, reliable and functional reseller-oriented provisioning and management platforms in our industry, and we continue to refine, evolve and improve these services for both resellers and end-users.

Our principal place of business is located in Canada. We report our financial results as one operating segment. Our chief operating decision maker regularly reviews our operating results on a consolidated basis, principally to make decisions about how we utilize our resources and to measure our consolidated operating performance. To assist us in forecasting growth and to help us monitor the effectiveness of our operational strategies, our chief operating decision maker regularly reviews revenue for each of our service offerings in order to gain more depth and understanding of the key business metrics driving our business. Accordingly, we report revenue in the following service areas:

OpenSRS, our wholesale service, manages over ten million domain names, under its ICANN accreditation and names Tucows manages for other registrars under their own accreditations, millions of mailboxes, tens of thousands of digital certificates and our billing service, Platypus through a network of over 11,000 web hosts, Internet service providers, or ISPs, and other resellers around the world.

Hover, our retail service, offers services similar to those of OpenSRS to consumers and small businesses.

YummyNames, our domain portfolio service, manages tens of thousands of domain names, most of which generate advertising revenue and many of which we offer for resale via our reseller network and other channels. Included in the YummyNames domain portfolio are over 42,000 domains that allow over two-thirds of Americans to purchase a domain or email address based on their name.

Butterscotch, our content service, operates two advertising-supported websites, butterscotch.com and tucows.com, which provide content to help consumers overcome the complexity of modern technology and the Internet, in the form of over 4,000 videos and over 385,000 software and mobile listings and articles. Additionally, Butterscotch provides custom video production services for technology manufacturers and ISPs.

Our business model is characterized by non-refundable, up-front payments, which lead to recurring revenue and positive operating cash flow.

For the years ended December 31, 2010, 2009 and 2008, we reported revenue of \$85 million, \$81 million and \$79 million, respectively. For the years ended December 31, 2010, 2009 and 2008, our OpenSRS domain service offering accounted for 77%, 73% and 69% of our total revenue, respectively.

**KEY BUSINESS METRICS**

We regularly review a number of business metrics, including the following key metrics to, assist us in evaluating our business, measure the performance of our business model, identify trends, determine resource allocations, formulate financial projections and make strategic business decisions. The



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following table sets forth, the key business metrics which we believe are the primary indicators of our performance for the periods presented:

|   | Year ended<br>December 31,(1) |       |       |
|---|-------------------------------|-------|-------|
|   | 2010                          | 2009  | 2008  |
|   | (in 000's)                    |       |       |
| Total new, renewed and transferred-in domain name registrations provisioned | 7,396                         | 6,654 | 6,006 |
| Domain names under management   |                               |       |       |
| Provisioned on behalf of Tucows   | 8,809                         | 8,128 | 7,694 |
| Provisioned on behalf of accredited registrars                              | 1,400                         | 1,567 | 1,449 |
| Total domain names under management   | 10,209                        | 9,695 | 9,143 |

- (1) For a discussion of these period to period changes in the domains provisioned and domains under management and how they impacted our financial results see the Net revenue discussion below.

**OPPORTUNITIES, CHALLENGES AND RISKS**

The increased competition in the market for Internet services in recent years, which the Company expects will continue to intensify in the short and long term, poses a material risk for the Company. As new registrars are introduced, existing competitors expand service offerings and competitors offer price discounts to gain market share, the Company faces pricing pressure, which can adversely impact its revenues and profitability. To address these risks, the Company has focused on leveraging the scalability of its infrastructure and its ability to provide proactive and attentive customer service to aggressively compete to attract new customers and to maintain existing customers.

Our direct costs to register domain names on behalf of our customers are almost exclusively controlled by registries such as Verisign and by ICANN. Verisign provides all the registry services operations for the .com, .net, .cc, .tv, and .name domain names. ICANN is a private sector, not-for-profit corporation formed to oversee a number of Internet related tasks, including domain registrations for which it collects fees. The market for wholesale registrar services is both price sensitive and competitive, particularly for large volume customers, such as large web hosting companies and owners of large portfolios of domain names. We have a relatively limited ability to increase the pricing of domain name registrations without negatively impacting our ability to maintain or grow our customer base.

In 2007, we entered into contractual agreements with Verisign for the supply of domain names. These agreements expire in 2012. Under the agreements, Verisign charges a fee for .com and .net domain names of \$7.34 and \$5.40 respectively, for each year for which a domain name is registered. In addition, in terms of Verisign's agreement with ICANN, Verisign has the right to increase the fee it charges for a .com or .net domain name by up to an additional 7% once in either 2011 or 2012. Mandated registry price increases such as this will adversely increase our service costs as a percentage of our total revenue. To implement this price increase however, Verisign is required to give registrars six months' notice.

In 2009, our contractual agreement with ICANN was amended to extend the terms of the agreement through June 30, 2014. Under the agreement, ICANN charges a \$0.18 fee for each year that a domain name is registered in the TLDs that fall within its purview. In addition, ICANN is currently deliberating on the timing and framework for a potentially significant expansion of the number of generic TLDs, or gTLDs. Although there can be no assurance that any gTLD expansion will occur, we believe that such expansion, if any, should result in an increase in the number of domains we register and related revenues.

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Our revenue is primarily realized in U.S. dollars and a major portion of our operating expenses are paid in Canadian dollars. Fluctuations in the exchange rate between the U.S. dollar and the Canadian dollar may have a material effect on our business, financial condition and results from operations. In particular, we may be adversely affected by a significant weakening of the U.S. dollar against the Canadian dollar on a quarterly and an annual basis. Our policy with respect to foreign currency exposure is to manage our financial exposure to certain foreign exchange fluctuations with the objective of neutralizing some or all of the impact of foreign currency exchange movements by entering into foreign exchange forward contracts to mitigate the exchange risk on a portion of our Canadian dollar exposure. We may not always enter into such forward contracts and such contracts may not always be available and economical for us. Additionally, the forward rates established by the contracts may be less advantageous than the market rate upon settlement.

Display advertising from the desk-top software download site has historically been the largest source of Butterscotch revenue. This revenue stream has suffered from the secular shift away from desktop software. Recently, we have experienced an increase in video advertising and corporate video revenue as advertisers continue to migrate their advertising spend towards more content rich websites such as Butterscotch.com. A portion of this increase was from larger video contracts which may not be repeatable. In addition, to reach a wider audience of consumers, Butterscotch has refocused its efforts towards mobile technology. We believe that these initiatives present us with a potentially larger long-term revenue opportunity. However, if our marketing efforts with the above initiatives, together with other initiatives we take to grow our revenue and our page views, are not successful in offsetting any decline we experience in display advertising from the desk-top software download site, in the short-term, may result in a decline in Butterscotch revenue.

**Net Revenues**

*OpenSRS*

We derive revenue from our reseller network by providing them with reseller services that comprise (a) domain service, (b) email service and (c) other services. Other services primarily consist of secure sockets layer, or SSL, certificates and also include blogware and website building tools that are used by our resellers to create bundles of Internet services for their end-users along with billing solutions for ISPs.

OpenSRS Domain Service

Historically, our OpenSRS domain service has constituted the largest portion of our business and encompasses all of our services as an accredited registrar related to the registration, renewal, transfer and management of domain names. In addition, this service fuels other revenue categories as it often is the initial service for which a customer will engage us, enabling us to follow on with other services and allowing us to add to our domain portfolio by purchasing names registered through us upon their expiration. We also provide resellers with the ability to sell personal names. This service allows resellers the opportunity to sell email addresses based on our domain portfolio of surname domain names.

As of December 31, 2010, we offer registration services for the generic top-level domain ("gTLDs") .com, .net, .org, .info, .name, .biz, .tel, .mobi and .asia and for the country code top-level domains ("ccTLDs") .at, .au, .be, .bz, .ca, .co, .cc, .ch, .cn, .de, .dk, .es, .eu, .fr, .in, .it, .li, .me, .mx, .nl, .tv, .uk, .ws, and .us.

With respect to the sale of domain registrations, our pricing structure for domain names provides visibility into the various fees that make up the cost of a domain name by breaking out the cost of the registry and ICANN fees separately from our management fee. Effective July 2010, registry fees for the .com and .net registrations were increased by the registry by an additional 7%. The management fee provides our resellers with access to our provisioning and management tools to enable them to

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register and administer domain names and access to additional services like WHOIS privacy and DNS services, enhanced domain name suggestion tools and access to our Premium Domain name services. We earn fees in connection with each new, renewed and transferred-in registration and from providing provisioning services to resellers and registrars on a monthly basis. Domain registrations are generally purchased for terms of one to ten years, with a majority having a one-year term. Except for certain large customers with whom we have negotiated alternative arrangements, payments for the full term of service, or billed revenue, is received at the time of activation of service. All fees received in connection with domain name registration are non-refundable, and where appropriate, are recorded as deferred revenue and recognized as earned ratably over the term of provision of service. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the quarters and the year.

OpenSRS Email Service

We derive revenue from our hosted email service through our global distribution network. Our email service is offered on a per account, per month basis, and provides resellers with a reliable, scalable "white label" hosted email solutions that can be customized to their branding and business model requirements. The email service also includes spam and virus filtering on all accounts. End-users can access the email service via a full-featured, multi-language AJAX-enabled web interface, a WAP mobile interface, or through traditional desktop email clients, such as Microsoft Outlook or Apple Mail, using IMAP or POP/SMTP and 2GB of email storage.

We earn fees for email services when such services are activated. Email services are generally purchased monthly and, at month-end, are either deducted on a pre-authorized basis from reseller's deposit account, or are invoiced.

Other OpenSRS Services

We derive revenue from other services primarily from provisioning SSL certificates. In addition, we provision blogware and website building tools that are used by our resellers to create bundles of Internet services for their end-users, as well as the provision of billing, provisioning and customer care software solutions to ISPs through our Platypus billing software.

We earn fees from such services when a service is activated. These services are generally purchased for terms of one month to three years. Platypus software is generally purchased for terms of one month to one year. Payments for services are for the full term of all services at the time of activation of service, are non-refundable and, where appropriate, are recorded as deferred revenue and recognized as earned ratably over the service term. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the quarters and the year.

*YummyNames*

We derive revenue from our portfolio of domain names by displaying advertising on the domains and by making them available for sale or lease. In addition we display advertising on "parked pages" within OpenSRS. Parked pages are domain names registered with us that do not yet contain an active website. When a user types one of these domain names into a web browser, they are presented with dynamically generated links that are pay-per-click advertising. Every time a user clicks on one of these links, it generates revenue for us through our partnership with third-parties who provide syndicated pay-per-click advertising.

Portfolio names are sold through our premium domain name service, auctions or in negotiated sales. The size of our domain name portfolio varies over time, as we acquire and sell domains on a regular basis to maximize the overall value and revenue generation potential of our portfolio. In evaluating names for sale, we consider the potential foregone revenue from pay-per-click advertising, as

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well as other factors. The name will be offered for sale if, based on our evaluation, the name is deemed non-essential to our business and management believes that deriving proceeds from the sale is strategically more beneficial to the Company.

Portfolio names that have been acquired from third-parties or through acquisition are included as intangible assets with indefinite lives on our consolidated balance sheet.

In addition, we also offer the same services to our customers, allowing them to make available names registered by them for monetization on a similar basis. For customer names, we earn a referral fee for premium names or names sold or leased, and participate on a revenue share basis for names offered through our pay-per-click advertising program.

We recognize revenue from these services, net of any fees payable to resellers or customers, immediately upon completion of the service, or in the case of advertising revenue, on a monthly basis once the advertising has been served.

*Hover*

We derive revenues from the providing and managing Internet services, on a retail basis, to consumers and small businesses through our Hover.com website. These services include domain registration and other Internet services such as email and personalized email through our portfolio of surname-based domain names, as well as an easy-to-use interface that allows users to connect domain names to websites and email addresses through a unique DNS forwarding system. Depending on the service offered, we typically receive fees for our services.

Our customers generally purchase services for terms of one to ten years, with a majority of services purchased for a one-year term. Certain services are also offered on a monthly basis. Payments for the full term of all services, or billed revenue, are received at the time of service activation and, where appropriate, are recorded as deferred revenue and recognized as earned ratably over the term of provision of service. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during quarterly and annual periods.

*Butterscotch*

We also generate advertising and other revenue through two ad-supported content sites, butterscotch.com and tu cows.com.

Butterscotch.com derives revenue from banner and text advertising on the site, as well as from video advertising and product placement within the videos that make up the bulk of the site. In addition, revenue is earned through custom video production for technology manufacturers and Internet services customers.

Tu cows.com advertising revenue is generated from third-party advertisers and from software developers who rely on us as a primary source of distribution. Software developers use our Author Resource Center to submit their products for inclusion on our site and to purchase promotional placement of their software. Software developers may also purchase other promotional services on a cost-per-click or flat rate basis. Software developers are able to promote their software through advertising services including keyword search placements, banners, promotional placements, expedited reviews and premium data services. Revenue is also generated from companies that contract with us to provide them with co-branded content.

Advertising and other revenue is recognized ratably over the period in which it is presented. To the extent that we do not meet the minimum number of post-presentation impressions that we guarantee to customers, we defer recognition of the corresponding revenues until the guaranteed impressions are

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achieved. Custom video production revenue is recognized on acceptance of the completed video by the customer.

**Critical Accounting Policies**

The following is a discussion of our critical accounting policies and methods. Critical accounting policies are defined as those that are both important to the portrayal of our financial condition and results of operations and are reflective of significant judgments and uncertainties made by management that may result in materially different results under different assumptions and conditions. Note 2 to the consolidated financial statements for the year ended December 31, 2010, or Fiscal 2010, includes further information on the significant accounting policies and methods used in the preparation of our consolidated financial statements.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate the application of these estimates, including those related to the recoverability of investments, useful lives and valuation of intangible assets, valuation of goodwill, fair value measurement of assets and liabilities, product development costs, revenue recognition and deferred revenue and accounting for income taxes. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual amounts could differ significantly from these estimates.

**Revenue recognition policy**

We earn revenues from the following services;

OpenSRS (Domain, Email and Other Services);

YummyNames;

Hover; and

Butterscotch.

With respect to the sale of domain registrations and other Internet services, we earn registration fees in connection with each new, renewed and transferred-in registration and from providing provisioning services to resellers and registrars on a monthly basis. We also enter into revenue arrangements in which a reseller may purchase a combination of services (multiple element arrangements). When fair value exists for all elements, we allocate revenue to each element based on the relative fair value of each of the elements. Fair value is established by the price charged when that element is sold separately. For arrangements where fair value exists only for the undelivered elements, we defer the fair value of the undelivered elements and recognize the difference between the total arrangement fee and the amount deferred for the undelivered items as revenue related to the delivered items, assuming all other criteria for revenue recognition have been met. Payments for the full term of all services, or billed revenue, are received at the time of activation of service and where appropriate are recorded as deferred revenue and are recognized as earned ratably over the term of provision of service. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the quarters and the year.

Revenue from the sale of domain names consists primarily of amounts earned for the transfer of rights to domain names that are currently under the Company's control. Collectability of revenues

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generated is subject to a high level of uncertainty; accordingly revenues are recognized only when payment is received.

We also generate advertising and other revenue through our online libraries of shareware, freeware and online services presented at our websites, [tucows.com](http://tucows.com) and [butterscotch.com](http://butterscotch.com). Advertising and other revenue is recognized ratably over the period in which it is presented. To the extent that the minimum number of impressions we guarantee to customers is not met, we defer recognition of the corresponding revenues until the guaranteed impressions are achieved. Custom video production revenue is recognized on acceptance of the completed video by the customer.

Changes to contractual relationships in the future could impact the amounts and timing of revenue recognition.

In those cases where payment is not received at the time of sale, additional conditions for recognition of revenue apply. The conditions are (i) that the collection of sales proceeds is reasonably assured and (ii) that we have no further performance obligations. We record expected refunds, rebates and credit card charge-backs as a reduction of revenues at the time of the sale based on historical experiences and current expectations. Should these expectations not be met, adjustments will be required in future periods.

We establish reserves for possible uncollectible accounts receivable and other contingent liabilities which may arise in the normal course of business. The allowance for doubtful accounts is calculated by taking into account factors such as our historical collection and write-off experience, the number of days the customer is past due and the status of the customer's account with respect to whether or not the customer is continuing to receive service. The contingent liability estimates are based on management's historical experience and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the reported amounts of liabilities and expenses that are not readily apparent from other sources. Historically, credit losses have been within our expectations and the reserves we have established have been appropriate. However, we have, on occasion, experienced issues which have led to accounts receivable not being fully collected. Should these issues occur more frequently, additional reserves may be required.

**Valuation of intangible assets, goodwill and long-lived assets**

Goodwill represents the excess of purchase price over the fair value of tangible or identifiable intangible assets acquired and liabilities assumed in the acquisitions noted below. Intangible assets consist of acquired technology, brand, customer relationships, non-competition agreements, surname domain names and direct navigation domain names. Intangible assets, comprising technology, brand value, customer relationships and non-competition arrangements related to the acquisition of Boardtown Corporation in April 2004, the acquisition of the Hosted Messaging Business of Critical Path, Inc. in January 2006, the acquisition of Mailbank.com Inc. in June 2006 and the acquisition of Innerwise, Inc. in July 2007, are being amortized on a straight-line basis over periods of two to seven years.

Goodwill and indefinite life intangibles are not amortized, but are tested for impairment annually or more frequently if circumstances indicate potential impairment, through a comparison of fair value to carrying amount. Goodwill is tested for impairment annually at the same time every year, and when an event occurs or circumstances change such that it is reasonably possible that impairment may exist. We review goodwill at least annually for possible impairment in the fourth quarter of each year.

We have other finite life intangible assets consisting of patented and non-patented technologies. These intangible assets are amortized over their expected economic lives. The lives are determined based upon the expected use of the asset, the estimated average life of the replacement parts of the

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reporting units products, the stability of the industry, expected changes in and replacement value of distribution networks and other factors deemed appropriate.

With regards to property, equipment and definite life intangible assets, we continually evaluate whether events or circumstances have occurred that indicate the remaining estimated useful lives of its definite-life intangible assets may warrant revision or that the remaining balance of such assets may not be recoverable. We measure recoverability of assets to be held and used by comparing the carrying amount of the assets to future undiscounted net cash flows expected to be generated by the assets. Recoverability measurement and estimation of undiscounted cash flows is done at the lowest possible levels for which there are identifiable cash flows. If such assets fail the recoverability test, the impairment to be recognized is measured as the amount by which the carrying amount of assets exceeds the fair value of the assets. Assets to be disposed of are recorded at the lower of the carrying amount or fair value less costs to sell. Management must exercise judgment in determining whether an event has occurred that may impair the value of the long-lived assets. Factors that could indicate that impairment may exist include significant underperformance relative to a plan or long-term projections, significant changes in business strategy, significant negative industry or economic trends or a significant decline in our stock price or in the value of our reporting units for a sustained period of time. There was no impairment recorded on definite-life intangible assets and property and equipment during 2010 and 2009.

Our 2010 annual goodwill impairment analysis, which we performed for our reporting unit as of December 31, 2010, did not result in an impairment charge. We determined the estimated fair value of our reporting unit using the income approach and the market approach to determine that the estimated fair value exceeded its carrying value. This analysis was consistent with the approach we utilized in our analysis performed in prior years. Determining the number of reporting units and the fair value of a reporting unit requires us to make judgments and involves the use of significant estimates and assumptions. These estimates and assumptions include revenue growth rates and operating margins used to calculate projected future cash flows, risk-adjusted discount rates, future economic and market conditions. The key assumptions used in our 2010 annual goodwill impairment test to determine the fair value of our reporting unit included: (a) cash flow projections, which include growth and allocation assumptions for forecasted revenue and expenses; (b) a residual growth rate of 3.0%; and (c) a discount rate of 18%, which was based upon our reporting unit's weighted-average cost of capital adjusted for the risks associated with the operations at the time of the assessment. As of the date of our 2010 annual impairment test, our estimated fair values for our reporting unit, based on reasonable changes in assumptions exceed its carrying value by a range of 40% to 80%. We believe that the assumptions and estimates used to determine the estimated fair value of our reporting unit are reasonable; however, these estimates are inherently subjective, and there are a number of factors, including factors outside of our control that could cause actual results to materially differ from our estimates. Changes in estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge.

Any changes to our key assumptions about our businesses and our prospects, or changes in market conditions, could cause the fair value of our reporting unit to fall below its carrying value, resulting in a potential impairment charge. In addition, changes in our organizational structure or how our management allocates resources and assesses performance, could result in a change in our operating segments or reporting units, requiring a reallocation and updated impairment analysis of goodwill. A goodwill or intangible asset impairment charge could have a material effect on our consolidated financial statements because of the significance of goodwill and intangible assets to our consolidated balance sheet. As of December 31, 2010, we had \$18.0 million and \$16.9 million, respectively, in goodwill and intangible assets.

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**Accounting for income taxes**

We are subject to income taxes in the U.S. and numerous foreign jurisdictions. Significant judgment is required in evaluating our uncertain tax positions and determining our provision for income taxes. We apply a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if on the weight of available evidence; it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit that is more than 50% likely to be realized upon settlement.

Although we believe we have adequately reserved for our uncertain tax positions, no assurance can be given that the final tax outcome of these matters will not be different. We adjust these reserves in light of changing facts and circumstances, such as the closing of a tax audit or the refinement of an estimate. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact the provision for income taxes in the period in which such determination is made.

As we account for income taxes under the asset and liability method, we recognize deferred tax assets or liabilities for the anticipated future tax effects of temporary differences between the financial statement basis and the tax basis of our assets and liabilities. We record a valuation allowance to reduce the net deferred tax assets when it is more likely than not that the benefit from the deferred tax assets will not be realized. In assessing the need for a valuation allowance, historical and future levels of income, expectations and risks associated with estimates of future taxable income and ongoing tax planning strategies are considered. In the event that it is determined that the deferred tax assets to be realized in the future would be in excess of the net recorded amount, an adjustment to the deferred tax asset valuation allowance would be recorded. This adjustment would increase income in the period that such determination was made. Likewise, should it be determined that all or part of a recorded net deferred tax asset would not be realized in the future, an adjustment to increase the deferred tax asset valuation allowance would be charged to income in the period that such determination would be made.

On a periodic basis, we evaluate the probability that our deferred tax asset balance will be recovered to assess its realizability. To the extent we believe it is more likely than not that some portion of our deferred tax assets will not be realized, we will increase the valuation allowance against the deferred tax assets. Realization of our deferred tax assets is dependent primarily upon future taxable income. Our judgments regarding future profitability may change due to future market conditions, changes in U.S. or international tax laws and other factors. These changes, if any, may require possible material adjustments to these deferred tax assets, impacting net income or net loss in the period when such determinations are made.



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The following table presents our net revenues, by revenue source:

|                               | <b>Year ended December 31,</b> |                      |
|-------------------------------|--------------------------------|----------------------|
|                               | <b>2010</b>                    | <b>2009</b>          |
| <b>OpenSRS:</b>               |                                |                      |
| Domain Services               | \$ 64,977,121                  | \$ 59,248,732        |
| Email Services                | 2,325,253                      | 3,636,866            |
| Other Services                | 4,368,781                      | 4,425,940            |
| <b>Total OpenSRS Services</b> | <b>71,671,155</b>              | <b>67,311,538</b>    |
| Yummy Names                   | 6,123,708                      | 6,623,292            |
| Hover                         | 4,559,833                      | 4,970,635            |
| Butterscotch                  | 2,223,809                      | 2,033,747            |
|                               | <b>\$ 84,578,505</b>           | <b>\$ 80,939,212</b> |
| Increase over prior period    | \$ 3,639,293                   |                      |
| Increase percentage           |                                | 4%                   |

The following table presents our revenues, by revenue source, as a percentage of total revenues:

|                               | <b>Year ended</b>   |             |
|-------------------------------|---------------------|-------------|
|                               | <b>December 31,</b> |             |
|                               | <b>2010</b>         | <b>2009</b> |
| <b>OpenSRS:</b>               |                     |             |
| Domain Services               | 77%                 | 73%         |
| Email Services                | 3%                  | 4%          |
| Other Services                | 5%                  | 6%          |
| <b>Total OpenSRS Services</b> | <b>85%</b>          | <b>83%</b>  |
| Yummy Names                   | 7%                  | 8%          |
| Hover                         | 5%                  | 6%          |
| Butterscotch                  | 3%                  | 3%          |
|                               | <b>100%</b>         | <b>100%</b> |

Total net revenues for Fiscal 2010 increased by \$3.7 million, or 4.5%, to \$84.6 million from \$80.9 million for the year ended December 31, 2009, or Fiscal 2009. Deferred revenue from domain name registrations and other Internet services at December 31, 2010 increased to \$62.6 million from \$56.3 million at December 31, 2009.

No customer accounted for more than 10% of revenue during Fiscal 2010 and, at December 31, 2010, three customers accounted for 35% of accounts receivable. Significant management judgment is required at the time of recording of revenue to assess whether the collection of the resulting receivables is reasonably assured. On an ongoing basis, we assess the ability of our customers to make required payments. Based on this assessment, we expect the carrying amount of our outstanding receivables, net of allowance for doubtful accounts, to be fully collected.

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***OpenSRS***

During Fiscal 2010, OpenSRS revenue increased by \$4.4 million to \$71.7 million when compared to Fiscal 2009 primarily as a result of OpenSRS domain revenue increasing by \$5.6 million or 10% to \$65.0 million. This increase resulted primarily from the impact of the 7% increase in registration fees paid to certain registries that were implemented in July 2010 and from our success in attracting large volume customers who have higher transaction volumes. This increase was partially offset by a decrease in email revenue by \$1.3 million or 36% to \$2.3 million, which was primarily attributable to the following two factors:

our decision to eliminate certain enterprise customers acquired as part of the Hosted Messaging Business of Critical Path, Inc. in January 2006 that were not part of our strategic focus and who were receiving pricing that was not competitive in the marketplaces; and

certain of our email customers, who are media portal companies and for whom email is only a small component of their overall service offerings, have chosen to include their email services as part of larger supply contracts for competitive and cost-control reasons. The last of these customers migrated away from our hosted email platform during the three months ended December 31, 2009. As our marketing efforts to date have not yet been successful in offsetting these customer losses, these customer losses have had a material impact on our results of operations for email services for Fiscal 2010.

During Fiscal 2010, the total new, renewed and transferred-in domain name registrations that we processed increased by 0.7 million to 7.4 million registrations as compared to Fiscal 2009. This increase resulted primarily from our continuing efforts to attract new clients and retain existing customers. While we anticipate that the number of new, renewed and transferred-in domain name registrations will continue to incrementally increase in the long term, the volatility in the market could affect the growth of domain names that we manage. In addition, new TLDs, including new IDN TLDs, ccTLDs and gTLDs, may be introduced by ICANN in 2011 and/or 2012. We cannot assess the impact, if any; the introduction of these new TLDs will have on our revenues and results of operations. See "Risk Factors".

As of December 31, 2010, the total domain names under our management had increased by 0.7 million to 8.8 million domain names, as compared to the total domain names under our management as of December 31, 2009. In addition, we provide provisioning services on a monthly basis to accredited registrars who use our technical systems to process domain registrations with their own accreditation. As of December 31, 2010, we managed 1.4 million domain names on behalf of other accredited registrars, a decrease of 0.2 million domain names compared to 1.6 million as of December 31, 2009. The decrease is primarily attributable to the loss of an accredited registrar who had 0.3 million domains under management with us who have transferred their domain registration business to a competitive registrar with whom they have a reciprocal supply arrangement.

***YummyNames***

Net revenues from our YummyNames domain portfolio service for Fiscal 2010 decreased by \$0.5 million, or 7.5%, to \$6.1 million compared to Fiscal 2009.

During Fiscal 2010, we earned \$4.9 million by making domain names in our portfolio available for sale or lease, compared to \$4.6 million during Fiscal 2009. In addition we earned \$1.2 million from our pay-per-click advertising or parked pages program during Fiscal 2010 compared to \$2.0 million for Fiscal 2009.

This decrease primarily reflects the decrease in the delivery of third-party advertisements on parked pages of \$0.8 million as a result of the impact our domain name sales have on our advertising

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revenue and the general economic conditions resulting in a generally slower advertising environment. These decreases have been partially offset by the timing of larger portfolio sales of domain.

The market for monetization of domain names is rapidly evolving and there is no guarantee that we will be able to continue to acquire the same caliber of names for our portfolio from future expiring domains or that names we acquire in future will provide the same revenue impact as we have experienced from past acquisitions. In addition, the revenue we derive from domain portfolio services is driven by general macroeconomic factors that affect internet advertising. Our advertising expenditures are typically sensitive to economic conditions and tend to decline in recessionary periods and other periods of economic uncertainty.

***Hover***

Net revenues from Hover for Fiscal 2010 as compared to Fiscal 2009 decreased by \$0.4 million, or 8%, to \$4.6 million.

This decrease resulted primarily from the significant development efforts that Hover undertook during Fiscal 2009. These development efforts resulted in a decrease in the deferred revenue balance during Fiscal 2009 as cash receipts added to deferred revenue during Fiscal 2009 were lower than the revenue being recognized from prior periods. Consequently, although cash receipts for Fiscal 2010 increased as compared to Fiscal 2009, net revenue decreased.

***Butterscotch***

Net revenues from Butterscotch for Fiscal 2010 as compared to Fiscal 2009 increased by \$0.2 million, or 9%, to \$2.2 million. This increase is primarily the result of increases in video advertising and corporate video revenue as advertisers continued to increase advertising spending on more content rich websites such as Butterscotch.com. A portion of this increase was from larger video contracts which may not be repeatable. This increase has been partially offset by the decline in our Author Resource Center, which we believe reflects the current preference of advertisers for more content rich websites, as well as the significant decrease we have experienced in Ad Sense revenue, which resulted from Google's elimination of their enterprise level AdSense program.

**COST OF REVENUES**

***OpenSRS***

*OpenSRS Domain Service*

Cost of revenues for domain registrations represents the amortization of registry fees on a basis consistent with the recognition of revenues from our customers, namely ratably over the term of provision of the service. Registry fees, the primary component of cost of revenues, are paid in full when the domain is registered, and are initially recorded as prepaid domain registry fees. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the period.

*OpenSRS Email Service*

Cost of revenues for email services are payable to third-party providers for licensing and royalty costs related to the provision of certain components of our email services. Fees payable for these components are included in the cost of revenues in the month they are incurred.

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*Other OpenSRS Services*

Costs of revenues for other reseller services include fees paid to third-party service providers, primarily for SSL certificates and for printing services in connection with Platypus. Fees payable for SSL certificates are amortized on a basis consistent with the provision of service, generally one year, while monthly printing fees are included in cost of revenues in the month they are incurred.

*YummyNames*

Costs of revenues for our domain portfolio service represent the amortization of registry fees for domains added to our portfolio over the renewal period, which is generally one year, the value attributed under intangible assets to any domain name sold and any impairment charges that may arise from our assessment of our domain name intangible assets. As the total names in our portfolio continue to grow, this cost will become a more significant component of our cost of revenues. Payments for domain registrations are payable for the full term of service at the time of activation of service and are recorded as prepaid domain registry fees and are expensed ratably over the renewal term.

*Hover*

Costs of revenues for our provision and management of Internet services on a retail basis include the amortization of registry fees on a basis consistent with the recognition of revenues from our customers, namely ratably over the term of provision of the service and includes the amortization of registry fees payable to renew the domains in our surname portfolio. Registry fees, the primary component of cost of revenues, are paid in full when the domain is registered, and are recorded as prepaid domain registry fees.

*Butterscotch*

Costs of revenues for our ad-supported content sites include the fees paid to third-party service providers, primarily for digital certificates sold through our content sites and content license fees.

*General*

As a significant portion of our expenses are incurred in Canadian dollars, the strengthening of the Canadian dollar relative to the U.S. dollar has negatively impacted operating expenses during Fiscal 2010 when compared to Fiscal 2009. Exchange rates are, however, subject to significant and rapid fluctuations, and therefore we cannot predict the prospective impact of exchange rate fluctuations on our business, results of operations and financial condition.

*Network costs*

Network costs include personnel and related expenses, depreciation and amortization, communication costs, equipment maintenance, stock-based compensation and employee and related costs directly associated with the management and maintenance of our network. Communication costs include bandwidth, co-location and provisioning costs we incur to support the supply of all our services.

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The following table presents our cost of revenues, by revenue source:

|  | Year ended December 31, |                      |
|--|-------------------------|----------------------|
|  | 2010                    | 2009                 |
| <b>OpenSRS:</b>                              |                         |                      |
| Domain Services                              | \$ 54,087,893           | \$ 48,202,033        |
| Email Services                               | 425,836                 | 546,455              |
| Other Services                               | 1,570,481               | 1,622,086            |
| <b>Total OpenSRS Services</b>                | <b>56,084,210</b>       | <b>50,370,574</b>    |
| Yummy Names                                  | 817,290                 | 847,269              |
| Hover  | 1,527,727               | 1,925,188            |
| Butterscotch                                 | 65,622                  | 44,886               |
| Network, other costs                         | 4,648,899               | 4,748,189            |
| Network, depreciation and amortization costs | 1,331,576               | 1,789,987            |
|  | <b>\$ 64,475,324</b>    | <b>\$ 59,726,093</b> |
| Increase over prior period                   | \$ 4,749,231            |                      |
| Increase percentage                          |                         | 8%                   |

The following table presents our cost of revenues, as a percentage of total cost of revenues for the periods presented:

|  | Year ended December 31, |             |
|--|-------------------------|-------------|
|  | 2010                    | 2009        |
| <b>OpenSRS:</b>                              |                         |             |
| Domain Services                              | 85%                     | 81%         |
| Email Services                               | 1%                      | 1%          |
| Other Services                               | 2%                      | 3%          |
| <b>Total OpenSRS Services</b>                | <b>88%</b>              | <b>85%</b>  |
| Yummy Names                                  | 1%                      | 1%          |
| Hover  | 2%                      | 3%          |
| Butterscotch                                 | 0%                      | 0%          |
| Network, other costs                         | 7%                      | 8%          |
| Network, depreciation and amortization costs | 2%                      | 3%          |
|  | <b>100%</b>             | <b>100%</b> |

Total cost of revenues for Fiscal 2010 increased by \$4.8 million, or 8%, to \$64.5 million from \$59.7 million in Fiscal 2009. Prepaid domain registration and other Internet services fees as of December 31, 2010 increased by \$6.1 million, or 14%, to \$49.8 million from \$43.7 million at December 31, 2009.

**OpenSRS**

Costs for OpenSRS for Fiscal 2010 increased by \$5.7 million, or 11% to \$56.1 million from \$50.4 million, when compared to Fiscal 2009. This increase was primarily the result of increased domain registration volume and the increases in July 2010 of registration fees paid to the registries. This increase was partially offset by certain one-time email service costs we incurred during Fiscal 2009.

Table of Contents***YummyNames***

Costs for YummyNames for Fiscal 2010 as compared to Fiscal 2009 remained relatively flat at \$0.8 million.

***Hover***

Costs for Hover for Fiscal 2010 as compared to Fiscal 2009 decreased by \$0.4 million, to \$1.5 million, and resulted primarily from the introduction of new email service products, such as our family plan, which have changed our sales mix such that email services, which have a relatively lower cost of sales, account for an increased proportion of our Hover costs.

***Network costs***

Network costs before depreciation and amortization for Fiscal 2010 decreased by \$0.1 million, or 2%, to \$4.6 million, primarily as a result of lower bandwidth, support contract and workforce costs. This occurred despite the significant strengthening, on average, of the Canadian dollar relative to the U.S. dollar by approximately 9% as compared to Fiscal 2009, and reflects our improved efficiency in operating and managing our co-location facilities.

Amortization of intangible assets consists of amounts arising in connection with the acquisition of technology from each of the Boardtown Corporation in April 2004, the hosted messaging business of Critical Path, Inc. in January 2006, Mailbank.com Inc. in June 2006 and IYD in July 2007.

The technology purchased in connection with the acquisition of Boardtown Corporation is amortized on a straight-line basis over seven years, and for IYD over three years, while the technology acquired in connection with each of the acquisitions of the hosted messaging assets of Critical Path, Inc. and the in-house software of Mailbank.com Inc. was amortized on a straight-line basis over two years.

We expect cost of sales to increase as a result of transactional volumes and the competitive and general business environment during Fiscal 2011.

**SALES AND MARKETING**

Sales and marketing expenses consist primarily of personnel costs. These costs include commissions and related expenses of our sales, product management, public relations, call center, support and marketing personnel. Other sales and marketing expenses include customer acquisition costs, advertising and other promotional costs.

|                            | Year ended December 31, |              |
|----------------------------|-------------------------|--------------|
|                            | 2010                    | 2009         |
| Sales and marketing        | \$ 7,217,754            | \$ 5,812,007 |
| Increase over prior period | \$ 1,405,747            |              |
| Increase percentage        | 24%                     |              |
| Percentage of net revenues | 9%                      | 7%           |

Sales and marketing expenses for Fiscal 2010 increased by \$1.4 million, or 24%, to \$7.2 million as compared to Fiscal 2009. This increase was primarily due to higher workforce costs that resulted from an increase in the number of people employed in both our marketing and customer service departments, undertaking additional marketing campaigns, participating in additional trade shows and the negative impact of the approximate 9% strengthening, on average, in the Canadian dollar relative to the U.S. dollar compared to Fiscal 2009.

Excluding movements in exchange rates, we expect sales and marketing expenses for the fiscal year ending December 31, 2011 to increase slightly, in absolute dollars, as we adjust our marketing programs and sales and customer support people costs to meet future opportunities in the marketplace.

Table of Contents**TECHNICAL OPERATIONS AND DEVELOPMENT**

Technical operations and development expenses consist primarily of personnel costs and related expenses required to support the development of new or enhanced service offerings and the maintenance and upgrading of existing infrastructure. This includes expenses incurred in the research, design and development of technology that we use to register domain names, email, retail, domain portfolio and other Internet services, as well as to distribute our digital content services. Editorial costs relating to the rating and review of the software content libraries are included in the costs of product development. All technical operations and development costs are expensed as incurred.

|                                      | Year ended December 31, |              |
|--------------------------------------|-------------------------|--------------|
|                                      | 2010                    | 2009         |
| Technical operations and development | \$ 4,577,898            | \$ 4,550,704 |
| Increase over prior period           | \$ 27,194               |              |
| Increase percentage                  | 1%                      |              |
| Percentage of net revenues           | 5%                      | 6%           |

Technical operations and development expenses for Fiscal 2010 remained relatively flat at \$4.6 million when compared to Fiscal 2009, primarily due to the productivity improvements that have resulted from our adoption of an agile development model, which deploys our development, quality assurance, product management and operations employees into smaller teams, offsetting the approximate 9% strengthening, on average, in the Canadian dollar relative to the U.S. dollar when compared to Fiscal 2009.

Excluding movements in exchange rates; we expect technical operations and development expenses for the fiscal year ending December 31, 2011, in absolute dollars, to increase slightly when compared to the fiscal year ended December 31, 2010.

**GENERAL AND ADMINISTRATIVE**

General and administrative expenses consist primarily of compensation and related costs for managerial and administrative personnel, fees for professional services, public listing expenses, rent, foreign exchange and other general corporate expenses.

|                            | Year ended December 31, |              |
|----------------------------|-------------------------|--------------|
|                            | 2010                    | 2009         |
| General and administrative | \$ 2,879,825            | \$ 5,558,921 |
| Decrease over prior period | \$ (2,679,096)          |              |
| Decrease percentage        | (48)%                   |              |
| Percentage of net revenues | 3%                      | 7%           |

General and administrative expenses for Fiscal 2010 decreased by \$2.7 million, or 48%, to \$2.9 million as compared to Fiscal 2009. This was primarily as a result of our recording a foreign exchange gain of \$2.3 million during Fiscal 2010 as compared to a foreign exchange loss of \$0.7 million during Fiscal 2009. This gain in foreign exchange was primarily the result of the strengthening, on average, of the Canadian dollar relative to the U.S. dollar by approximately 9% from Fiscal 2009. This decrease was offset mainly by an increase in workforce related costs, facility costs and professional services of \$0.3 million during Fiscal 2010, as compared to Fiscal 2009.

Excluding movements in exchange rates; we expect general and administrative expenses for the fiscal year ending December 31, 2011, in absolute dollars, to increase slightly when compared to the fiscal year ended December 31, 2010.

Table of Contents**DEPRECIATION OF PROPERTY AND EQUIPMENT**

Property and equipment is depreciated on a straight-line basis over the estimated useful lives of the assets.

|  | Year ended December 31, |           |
|--|-------------------------|-----------|
|  | 2010                    | 2009      |
| Depreciation of property and equipment | \$170,844               | \$266,251 |
| Decrease over prior period             | \$(95,407)              |           |
| Decrease percentage                    | (36)%                   |           |
| Percentage of net revenues             | 0%                      | 0%        |

Depreciation costs for Fiscal 2010 decreased by \$0.1 million, or 36%, to \$0.2 million, primarily as a result of certain of our older assets becoming fully depreciated.

**LOSS ON DISPOSITION OF PROPERTY AND EQUIPMENT**

|   | Year ended<br>December 31, |          |
|---|----------------------------|----------|
|   | 2010                       | 2009     |
| Loss on disposition of property and equipment | \$                         | \$40,893 |

As part of our ongoing initiatives to improve the efficiency of our production environment, we retired some older computer hardware at our co-location facilities during Fiscal 2009, which resulted in a loss on the disposition of such equipment.

**AMORTIZATION OF INTANGIBLE ASSETS**

|                                   | Year ended December 31, |              |
|-----------------------------------|-------------------------|--------------|
|                                   | 2010                    | 2009         |
| Amortization of intangible assets | \$ 1,442,160            | \$ 1,442,160 |
| Decrease over prior period        | \$                      |              |
| Decrease percentage               |                         | %            |
| Percentage of net revenues        | 2%                      | 2%           |

Amortization of intangible assets consists of amounts arising in connection with the acquisition of Boardtown in April 2004, from the acquisition of the Hosted Messaging Assets of Critical Path, Inc. in January 2006, the acquisition of Mailbank.com Inc. in June 2006 and the acquisition of Innerwise, Inc. in July 2007.

The brand and customer relationships acquired in connection with the acquisition of Boardtown Corporation are amortized on a straight-line basis over seven years.

Customer relationships acquired in connection with the acquisition of the Hosted Messaging Assets of Critical Path, Inc. is amortized on a straight-line basis over five years.

Customer relationships acquired in connection with the acquisition of Mailbank.com Inc. are amortized on a straight-line basis over five years.

The brand and customer relationships acquired in connection with the acquisition of Innerwise, Inc. are amortized on a straight-line basis over seven years.



Table of Contents**LOSS (GAIN) IN FAIR VALUE OF FORWARD EXCHANGE CONTRACTS**

Although our functional currency is the U.S. dollar, a major portion of our fixed expenses are incurred in Canadian dollars. Our goal with regard to foreign currency exposure is, to the extent possible; to achieve operational cost certainty, manage financial exposure to certain foreign exchange fluctuations and to neutralize some of the impact of foreign currency exchange movements. Accordingly, we enter into foreign exchange contracts to mitigate the exchange rate risk on portions of our Canadian dollar exposure.

As we did not comply with the documentation requirements for hedge accounting, we account for the fair value of the derivative instruments within the consolidated balance sheet as a derivative financial asset or liability and the corresponding change in fair value is recorded in the consolidated statement of operations.

|  | Year ended December 31, |                |
|--|-------------------------|----------------|
|  | 2010                    | 2009           |
| Loss (gain) in fair value of forward contracts | \$ 1,370,710            | \$ (4,179,589) |
| Increase over prior period                     | \$ 5,550,299            |                |
| Increase percentage                            | (133)%                  |                |
| Percentage of net revenues                     | 2%                      | (5)%           |

We have entered into forward exchange contracts to meet a portion of our future Canadian dollar requirements through November 2011. The impact of the fair value adjustment on unrealized foreign exchange on these contracts for Fiscal 2010 was a net loss of \$1.4 million, as compared to a net gain of \$4.2 million for Fiscal 2009. This net loss in fair value of forward contracts results from a combination of the impact from the change in foreign exchange rates over time, as well as from the impact of the settlement of forward exchange contracts as they mature.

At December 31, 2010, our balance sheet reflects a derivative instrument asset of \$0.8 million as a result of our existing foreign exchange contracts we have entered into. Until their respective maturity dates, these contracts will fluctuate in value in line with movements in the Canadian vs. U.S. dollar.

**OTHER INCOME AND EXPENSES**

|                             | Year ended December 31, |              |
|-----------------------------|-------------------------|--------------|
|                             | 2010                    | 2009         |
| Other income (expense), net | \$ (116,197)            | \$ 4,268,050 |
| Decrease over prior period  | \$ (4,384,247)          |              |
| Decrease percentage         | (103)%                  |              |
| Percentage of net revenues  | (0)%                    | 5%           |

Other income (expense), net, decreased by \$4.4 million, or 103%, to \$0.1 million other expense from \$4.3 million other income as compared to Fiscal 2009.

The net decrease in other income during Fiscal 2010 when compared to Fiscal 2009 was primarily the result of our recording a gain on the sale of our investment in Afiliac of \$3.9 million during Fiscal 2009.

In addition, in June 2009 we received an additional payment of \$0.6 million in connection with the Infonautics patents that we assigned in 2002 to a third party. In connection with the assignment of these patents, we retained the right to share in certain revenue relating to any cash flow received by the third party with respect to the commercialization of these patents. As the third party's costs of commercializing the patents are expected to increase in the future, we do not expect any future revenue received to be material.

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Also, net interest expense decreased by \$0.1 million during Fiscal 2010 when compared to the Fiscal 2009, primarily as a result of the monthly capital repayments of \$0.2 million and the annual cash sweep payment of \$0.7 million we made in April 2009 pursuant to the terms of our Bank of Montreal credit facility.

**INCOME TAXES**

The following table presents our provision for income taxes for the periods presented:

|  | Year ended December 31, |              |
|--|-------------------------|--------------|
|  | 2010                    | 2009         |
| Provision for (recovery of) income taxes | \$ 210,845              | \$ (251,384) |

Our provision for income taxes primarily relates to tax on current year taxable income of \$0.2 million; and tax expense of \$0.1 million related to revisions to prior year estimates; offsetting a benefit of \$50,311 related to investment tax credits earned during the period. We operate in various tax jurisdictions, and accordingly, our income is subject to varying rates of tax. Losses incurred in one jurisdiction cannot be used to offset income taxes payable in another jurisdiction. Our ability to use income tax loss carryforwards and future income tax deductions is dependent upon our operations in the tax jurisdictions in which such losses or deductions arise.

Our 2009 provision for income taxes primarily relates to prior year profits of \$0.5 million, tax expense of \$0.1 million related to revisions to prior year estimates; a benefit of \$0.6 million related to a reduction in the Company's recorded deferred tax liability and a benefit of \$0.3 million related to investment tax credits earned during the period.

Tucows has approximately \$0.2 million of total gross unrecognized tax benefit as of December 31, 2010 and \$0.1 million of total gross unrecognized tax benefit as of December 31, 2009, which if recognized would favorably affect the income tax rate in future periods. The unrecognized tax benefit relates to prior year Pennsylvania state franchise taxes and other US state taxes and tax credits in respect of Tucows expected 2010 research and development claim. Tucows will record the tax benefit of the 2010 research and development claim once it has reasonable assurance that it is more likely than not that all or a portion of the benefit arising from the claim will be realized.

A reconciliation of the federal statutory income tax rate to our effective tax rate is set forth in Note 11 of Notes to Consolidated Financial Statements included in this Annual Report on Form 10-K.

Table of Contents**RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2009 AS COMPARED TO THE YEAR ENDED DECEMBER 31, 2008****NET REVENUES**

The following table presents our net revenues, by revenue source:

|                               | <b>Year ended December 31,</b> |                      |
|-------------------------------|--------------------------------|----------------------|
|                               | <b>2009</b>                    | <b>2008</b>          |
| <b>OpenSRS:</b>               |                                |                      |
| Domain Services               | \$ 59,248,732                  | \$ 53,966,640        |
| Email Services                | 3,636,866                      | 5,765,223            |
| Other Services                | 4,425,940                      | 4,476,676            |
| <b>Total OpenSRS Services</b> | <b>67,311,538</b>              | <b>64,208,539</b>    |
| Yummy Names                   | 6,623,292                      | 4,896,943            |
| Hover                         | 4,970,635                      | 7,194,352            |
| Butterscotch                  | 2,033,747                      | 2,168,046            |
|                               | <b>\$ 80,939,212</b>           | <b>\$ 78,467,880</b> |
| Increase over prior period    | \$ 2,471,332                   |                      |
| Increase percentage           | 3%                             |                      |

The following table presents our revenues, by revenue source, as a percentage of total revenues:

|                               | <b>Year ended</b>   |             |
|-------------------------------|---------------------|-------------|
|                               | <b>December 31,</b> |             |
|                               | <b>2009</b>         | <b>2008</b> |
| <b>OpenSRS:</b>               |                     |             |
| Domain Services               | 73%                 | 69%         |
| Email Services                | 4%                  | 7%          |
| Other Services                | 6%                  | 6%          |
| <b>Total OpenSRS Services</b> | <b>83%</b>          | <b>82%</b>  |
| Yummy Names                   | 8%                  | 6%          |
| Hover                         | 6%                  | 9%          |
| Butterscotch                  | 3%                  | 3%          |
|                               | <b>100%</b>         | <b>100%</b> |

Total net revenues for Fiscal 2009 increased by \$2.5 million, or 3%, to \$80.9 million from \$78.5 million for the year ended December 31, 2008, or Fiscal 2008. Deferred revenue from domain name registrations and other Internet services at December 31, 2009 increased to \$56.3 million from \$54.2 million at December 31, 2008.

No customer accounted for more than 10% of revenue during Fiscal 2009 and, at December 31, 2009, one customer accounted for 11% of accounts receivable. Significant management judgment is required at the time of recording of revenue to assess whether the collection of the resulting receivables is reasonably assured. On an ongoing basis, we assess the ability of our customers to make required payments. Based on this assessment, we expect the carrying amount of our outstanding receivables, net of allowance for doubtful accounts, to be fully collected.

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***OpenSRS***

During Fiscal 2009, OpenSRS revenue increased by \$3.1 million to \$67.3 million when compared to Fiscal 2008.

The main contributor to this increase was domain services revenue, which increased by \$5.3 million to \$59.2 million, primarily as a result of the impact of the 7% registry price increase that was levied by some of our domain name suppliers in October 2008 and from our continuing to aggressively compete to attract new clients and retain existing customers.

This increase was partially offset by a decrease in email services revenue of \$2.1 million to \$3.6 million when compared to Fiscal 2008. As previously disclosed, this decrease in email service revenue is primarily attributable to two factors:

our decision to eliminate certain enterprise customers acquired as part of the Hosted Messaging Business of Critical Path, Inc. in January 2006 that were not part of our strategic focus and who were receiving pricing that was not competitive in the marketplaces; and

certain of our email customers, who are media portal companies and for whom email is only a small component of their overall service offerings, have chosen to include their email services as part of larger supply contracts for competitive and cost-control reasons. The last of these customers migrated away from our hosted email platform during the three months ended December 31, 2009. As our marketing efforts to date have not yet been successful in offsetting these customer losses, these customer losses have had a material impact on our results of operations for email services for Fiscal 2009.

During Fiscal 2009, the total new, renewed and transferred-in domain name registrations that we processed increased by 0.7 million to 6.7 million registrations as compared to Fiscal 2008. This increase resulted primarily from our continuing to aggressively compete to attract new clients and retain existing customers.

As of December 31, 2009, the total domain names under our management had increased by 0.4 million to 8.1 million domain names, as compared to the total domain names under our management as of December 31, 2008. In addition, we provide provisioning services on a monthly basis to accredited registrars who use our technical systems to process domain registrations with their own accreditation. As of December 31, 2009, we managed 1.6 million domain names on behalf of other accredited registrars, an increase of 0.2 million domain names compared to the 1.4 million as of December 31, 2008.

***YummyNames***

Net revenues from our YummyNames domain portfolio service for Fiscal 2009 increased by \$1.7 million, or 35%, to \$6.6 million compared to Fiscal 2008.

During Fiscal 2009, we earned \$4.6 million by making domain names in our portfolio available for sale or lease, compared to \$2.0 million during Fiscal 2008. In addition we earned \$2.0 million from our pay-per-click advertising or parked pages program during Fiscal 2009 compared to \$2.9 million for Fiscal 2008.

This increase primarily reflects the timing of larger portfolio sales of domain names as well as the improved performance we are currently experiencing with our auction initiatives. These increases have been partially offset by the decrease in the delivery of third-party advertisements on parked pages of \$0.9 million as a result of the impact our domain name sales have on our advertising revenue and the general economic conditions resulting in a generally slower advertising environment.

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The market for monetization of domain names is rapidly evolving and there is no guarantee that we will be able to grow revenue at the rate achieved during Fiscal 2009, nor that we will be able to continue to acquire the same caliber of names for our portfolio from future expiring domains or that names we acquire in future will provide the same revenue impact as we have experienced from past acquisitions. In addition, the revenue we derive from domain portfolio services is driven by general macroeconomic factors that affect internet advertising. Our advertising expenditures are typically sensitive to economic conditions and tend to decline in recessionary periods and other periods of economic uncertainty. A slowing economy may thus be accompanied by a decrease in advertising spending which could adversely impact our ability to grow or maintain our domain portfolio services revenue.

***Hover***

Net revenues from Hover for Fiscal 2009 as compared to Fiscal 2008 decreased by \$2.2 million, or 31%, to \$5.0 million.

This decrease primarily resulted from the impact of the sale of our retail hosting assets during Fiscal 2008 on current year revenues. To a lesser extent, our decisions to reclassify certain retail customers acquired in the IYD acquisition that did not meet our definition of retail customers to OpenSRS and de-emphasize new customer acquisitions while we transitioned our retail customers from our Domain Direct, NetIdentity and IYD services to Hover also contributed to this decrease.

***Butterscotch***

Net revenues from Butterscotch for Fiscal 2009 as compared to Fiscal 2008 decreased by \$0.1 million, or 6%, to \$2.0 million. This decrease is primarily a result of the contraction in the yields from our syndicated Google feeds, and decreased revenue from our Author Resource Center of \$0.3 million. This decrease was partially offset by an increase in advertising and video revenue of \$0.2 million.

**COST OF REVENUES**

***OpenSRS***

*OpenSRS Domain Service*

Cost of revenues for domain registrations represents the amortization of registry fees on a basis consistent with the recognition of revenues from our customers, namely ratably over the term of provision of the service. Registry fees, the primary component of cost of revenues, are paid in full when the domain is registered, and are initially recorded as prepaid domain registry fees. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the period.

*OpenSRS Email Service*

Cost of revenues for email services are payable to third-party providers for licensing and royalty costs related to the provision of certain components of our email services. Fees payable for these components are included in the cost of revenues in the month they are incurred.

*Other OpenSRS Services*

Costs of revenues for other reseller services include fees paid to third-party service providers, primarily for SSL certificates and for printing services in connection with Platypus. Fees payable for SSL certificates are amortized on a basis consistent with the provision of service, generally one year, while monthly printing fees are included in cost of revenues in the month they are incurred.

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***YummyNames***

Costs of revenues for our domain portfolio service represent the amortization of registry fees for domains added to our portfolio over the renewal period, which is generally one year, the value attributed under intangible assets to any domain name sold and any impairment charges that may arise from our assessment of our domain name intangible assets. Payments for domain registrations are payable for the full term of service at the time of activation of service and are recorded as prepaid domain registry fees and are expensed ratably over the renewal term.

***Hover***

Costs of revenues for our provision and management of Internet services on a retail basis include the amortization of registry fees on a basis consistent with the recognition of revenues from our customers, namely ratably over the term of provision of the service and includes the amortization of registry fees payable to renew the domains in our surname. Registry fees, the primary component of cost of revenues, are paid in full when the domain is registered, and are recorded as prepaid domain registry fees.

***Butterscotch***

Costs of revenues for our ad-supported content sites include the fees paid to third-party service providers, primarily for digital certificates sold through our content sites and content license fees.

***General***

As a significant portion of our expenses are incurred in Canadian dollars, the weakening of the Canadian dollar relative to the U.S. dollar has positively impacted network costs, sales and marketing expenses, technical operations and development expenses and general and administrative expenses during Fiscal 2009 when compared to Fiscal 2008. Exchange rates are, however, subject to significant and rapid fluctuations, and therefore we cannot predict the prospective impact of exchange rate fluctuations on our business, results of operations and financial condition.

***Network costs***

Network costs include personnel and related expenses, depreciation and amortization, communication costs, equipment maintenance, stock-based compensation and employee and related costs directly associated with the management and maintenance of our network. Communication costs include bandwidth, co-location and provisioning costs we incur to support the supply of all our services.

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The following table presents our cost of revenues, by revenue source:

|  | Year ended December 31, |                      |
|--|-------------------------|----------------------|
|  | 2009                    | 2008                 |
| <b>OpenSRS:</b>                              |                         |                      |
| Domain Services                              | \$ 48,202,033           | \$ 42,854,184        |
| Email Services                               | 546,455                 | 340,048              |
| Other Services                               | 1,622,086               | 1,629,894            |
| <b>Total OpenSRS Services</b>                | <b>50,370,574</b>       | <b>44,824,126</b>    |
| Yummy Names                                  | 847,269                 | 716,627              |
| Hover  | 1,925,188               | 2,272,532            |
| Butterscotch                                 | 44,886                  | 29,195               |
| Network, other costs                         | 4,748,189               | 6,771,556            |
| Network, depreciation and amortization costs | 1,789,987               | 3,073,649            |
|  | <b>\$ 59,726,093</b>    | <b>\$ 57,687,685</b> |
| Increase over prior period                   | \$ 2,038,408            |                      |
| Increase percentage                          |                         | 4%                   |

The following table presents our cost of revenues, as a percentage of total cost of revenues for the periods presented:

|  | Year ended December 31, |             |
|--|-------------------------|-------------|
|  | 2009                    | 2008        |
| <b>OpenSRS:</b>                              |                         |             |
| Domain Services                              | 81%                     | 74%         |
| Email Services                               | 1%                      | 1%          |
| Other Services                               | 3%                      | 3%          |
| <b>Total OpenSRS Services</b>                | <b>85%</b>              | <b>78%</b>  |
| Yummy Names                                  | 1%                      | 1%          |
| Hover  | 3%                      | 4%          |
| Butterscotch                                 | 0%                      | 0%          |
| Network, other costs                         | 8%                      | 12%         |
| Network, depreciation and amortization costs | 3%                      | 5%          |
|  | <b>100%</b>             | <b>100%</b> |

Total cost of revenues for Fiscal 2009 increased by \$2.0 million, or 4%, to \$59.7 million from \$57.7 million Fiscal 2008 or Fiscal 2008. Prepaid domain registration and other Internet services fees as of December 31, 2009 increased by \$2.7 million, or 6%, to \$43.7 million from \$41.1 million at December 31, 2008.

**OpenSRS**

Costs for OpenSRS for Fiscal 2009 increased by \$5.5 million, or 12% to \$50.4 million from \$44.8 million, when compared to Fiscal 2008. Higher domain registration volumes and increases in registration fees paid to the registries that were implemented in October 2008 accounted for \$5.3 million of this increase for Fiscal 2009 when compared to Fiscal 2008. Included in this increase is \$4.0 million related to the price increases noted above. As a result of a further price increase announced by Verisign on December 17, 2009, registry fees for .com and .net increased by an

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additional 7% effective July 1, 2010. In addition, \$0.2 million of the increase resulted from licensing and royalty costs payable to third-party service providers for email services.

***YummyNames***

Costs for YummyNames for Fiscal 2009 as compared to Fiscal 2008 increased by \$0.1 million, to \$0.8 million, as a result of the registry price increases. This was partially offset as a result of the total number of names in our portfolio declining, primarily as a result of the sale of domain names.

***Hover***

Costs for Hover for Fiscal 2009 as compared to Fiscal 2008 decreased by \$0.3 million, to \$1.9 million, and primarily reflects the lower revenue experienced during the year as well as the impact that the sale of our retail hosting assets during the 2008 fiscal year has had on our retail cost structure.

***Network costs***

Network costs before depreciation and amortization for Fiscal 2009 decreased by \$2.0 million, or 30%, to \$4.7 million, primarily as a result of lower bandwidth, support contract and workforce costs. The decrease is primarily attributable to the lower co-location costs stemming from the closure and relocation of our U.S.-based co-location facilities during September 2008 and the restructuring we implemented in November 2008. Network depreciation and amortization costs for Fiscal 2009 decreased by \$1.3 million, or 42%, to \$1.8 million, primarily as a result of certain of our older computer hardware being fully depreciated and not requiring replacement.

In addition, as a significant portion of our expenses are incurred in Canadian dollars, the weakening of the Canadian dollar relative to the U.S. dollar has positively impacted network costs during Fiscal 2009 when compared to Fiscal 2008. Exchange rates are, however, subject to significant and rapid fluctuations, and therefore we cannot predict the prospective impact of exchange rate fluctuations on our business, results of operations and financial condition.

Amortization of intangible assets consists of amounts arising in connection with the acquisition of technology from each of the Boardtown Corporation in April 2004, the hosted messaging business of Critical Path, Inc. in January 2006, Mailbank.com Inc. in June 2006 and IYD in July 2007.

The technology purchased in connection with the acquisition of Boardtown Corporation is amortized on a straight-line basis over seven years, and for IYD over three years, while the technology acquired in connection with each of the acquisitions of the hosted messaging assets of Critical Path, Inc. and the in-house software of Mailbank.com Inc. was amortized on a straight-line basis over two years.

**SALES AND MARKETING**

Sales and marketing expenses consist primarily of personnel costs. These costs include commissions and related expenses of our sales, product management, public relations, call center, support and marketing personnel. Other sales and marketing expenses include customer acquisition costs, advertising and other promotional costs.

|                            | <b>Year ended December 31,</b> |              |
|----------------------------|--------------------------------|--------------|
|                            | <b>2009</b>                    | <b>2008</b>  |
| Sales and marketing        | \$ 5,812,007                   | \$ 6,668,884 |
| Decrease over prior period | \$ (856,877)                   |              |
| Decrease percentage        | (13)%                          |              |
| Percentage of net revenues | 7%                             | 8%           |



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Sales and marketing expenses for Fiscal 2009 decreased by \$0.9 million, or 13%, to \$5.8 million as compared to Fiscal 2008. This decrease was primarily due to lower workforce costs that resulted from the restructuring we undertook in November 2008. This decrease was partially offset by an increase in marketing and travel related costs of \$0.1 million for Fiscal 2009, as compared to Fiscal 2008.

**TECHNICAL OPERATIONS AND DEVELOPMENT**

Technical operations and development expenses consist primarily of personnel costs and related expenses required to support the development of new or enhanced service offerings and the maintenance and upgrading of existing infrastructure. This includes expenses incurred in the research, design and development of technology that we use to register domain names, email, retail, domain portfolio and other Internet services, as well as to distribute our digital content services. Editorial costs relating to the rating and review of the software content libraries are included in the costs of product development. All technical operations and development costs are expensed as incurred.

|                                      | Year ended December 31, |              |
|--------------------------------------|-------------------------|--------------|
|                                      | 2009                    | 2008         |
| Technical operations and development | \$ 4,550,704            | \$ 6,172,428 |
| Decrease over prior period           | \$ (1,621,724)          |              |
| Decrease percentage                  | (26)%                   |              |
| Percentage of net revenues           | 6%                      | 8%           |

Technical operations and development expenses for Fiscal 2009 decreased by \$1.6 million, or 26%, to \$4.6 million as compared to Fiscal 2008.

This decrease for Fiscal 2009 resulted primarily from a decrease in workforce-related costs, including contract and outside service costs that resulted from the restructuring we undertook in November 2008.

**GENERAL AND ADMINISTRATIVE**

General and administrative expenses consist primarily of compensation and related costs for managerial and administrative personnel, fees for professional services, public listing expenses, rent and other general corporate expenses.

|                            | Year ended December 31, |              |
|----------------------------|-------------------------|--------------|
|                            | 2009                    | 2008         |
| General and administrative | \$ 5,558,921            | \$ 6,809,601 |
| Decrease over prior period | \$ (1,250,680)          |              |
| Decrease percentage        | (18)%                   |              |
| Percentage of net revenues | 7%                      | 9%           |

General and administrative expenses for Fiscal 2009 decreased by \$1.3 million, or 18%, to \$5.6 million as compared to Fiscal 2008.

General and administrative expenses decreased during Fiscal 2009 compared to Fiscal 2008 primarily as a result a decrease in net bank charges of \$0.9 million as a result of our initiative introduced in January 2009 to recover payment processing fees, a reduction in professional fees of \$0.4 million and a decrease in facility costs, telephone, investor and public relations costs of \$0.3 million. In addition to these decreases, we recognized a foreign exchange loss of \$0.7 million during Fiscal 2009 as compared to a foreign exchange loss of \$0.8 million during Fiscal 2008. This \$0.1 million decrease was primarily due to the impact of translating our Canadian dollar net assets on hand at December 31, 2009, to our functional currency of U.S. dollars. This impact has resulted from the significant weakening of the Canadian dollar relative to the U.S. dollar compared to Fiscal 2008. In

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addition, these decreases were offset by general and administrative expenses increasing by \$0.4 million as a result of additional public listing and workforce related costs incurred during the period.

**DEPRECIATION OF PROPERTY AND EQUIPMENT**

Property and equipment is depreciated on a straight-line basis over the estimated useful lives of the assets.

|  | Year ended December 31, |            |
|--|-------------------------|------------|
|  | 2009                    | 2008       |
| Depreciation of property and equipment | \$ 266,251              | \$ 263,745 |
| Increase over prior period             | \$ 2,506                |            |
| Increase percentage                    | 1%                      |            |

Depreciation remained relatively flat at \$0.3 million during Fiscal 2009 compared to Fiscal 2008.

**LOSS ON DISPOSITION OF PROPERTY AND EQUIPMENT**

|   | Year ended<br>December 31, |            |
|---|----------------------------|------------|
|   | 2009                       | 2008       |
| Loss on disposition of property and equipment | \$ 40,893                  | \$ 498,529 |

As part of our ongoing initiatives to improve the efficiency of our production environment, we retired some older computer hardware at our co-location facilities during Fiscal 2009, which resulted in a loss on the disposition of such equipment of \$41,000.

**AMORTIZATION OF INTANGIBLE ASSETS**

|                                   | Year ended December 31, |              |
|-----------------------------------|-------------------------|--------------|
|                                   | 2009                    | 2008         |
| Amortization of intangible assets | \$ 1,442,160            | \$ 1,483,195 |
| Decrease over prior period        | \$ (41,035)             |              |
| Decrease percentage               | (3)%                    |              |

Amortization of intangible assets consists of amounts arising in connection with the acquisition of Boardtown in April 2004, from the acquisition of the Hosted Messaging Assets of Critical Path, Inc. in January 2006, the acquisition of Mailbank.com Inc. in June 2006 and the acquisition of Innerwise, Inc. in July 2007.

In connection with the acquisition of Boardtown Corporation, the brand and customer relationships purchased are amortized on a straight-line basis over seven years.

Customer relationships acquired in connection with the acquisition of the Hosted Messaging Assets of Critical Path, Inc. is amortized on a straight-line basis over five years.

In connection with the acquisition of Mailbank.com Inc., customer relationships purchased are amortized on a straight-line basis over five years.

In connection with the acquisition of Innerwise, Inc., the brand and customer relationships purchased are amortized on a straight-line basis over seven years.

Table of Contents**LOSS (GAIN) IN FAIR VALUE OF FORWARD EXCHANGE CONTRACTS**

Although our functional currency is the U.S. dollar, a major portion of our fixed expenses are incurred in Canadian dollars. Our goal with regard to foreign currency exposure is, to the extent possible; to achieve operational cost certainty, manage financial exposure to certain foreign exchange fluctuations and to neutralize some of the impact of foreign currency exchange movements. Accordingly, we enter into foreign exchange contracts to mitigate the exchange rate risk on portions of our Canadian dollar exposure.

As we did not comply with the documentation requirements for hedge accounting, we account for the fair value of the derivative instruments within the consolidated balance sheet as a derivative financial asset or liability and the corresponding change in fair value is recorded in the consolidated statement of operations.

|  | <b>Year ended December 31,</b> |              |
|--|--------------------------------|--------------|
|  | <b>2009</b>                    | <b>2008</b>  |
| Loss (gain) in fair value of forward contracts | \$ (4,179,589)                 | \$ 1,974,919 |
| (Decrease) increase over prior period          | \$ (6,154,508)                 |              |

We have entered into forward exchange contracts to meet a portion of our future Canadian dollar requirements through April 2011. The impact of the fair value adjustment on unrealized foreign exchange on these contracts for Fiscal 2009 was a net gain of \$4.2 million, as compared to a net loss of \$2.0 million for Fiscal 2008. This net gain in fair value of forward contracts results from a combination of the impact from the change in foreign exchange rates over time, as well as from the impact of the settlement of forward exchange contracts as they mature.

At December 31, 2009, we reflect a derivative instrument asset of \$2.2 million on our balance sheet as a result of the foreign exchange contracts we have entered into. Until their respective maturity dates, these contracts will fluctuate in value in line with movements in the Canadian vs. U.S. dollar.

**OTHER INCOME AND EXPENSES**

|                            | <b>Year ended December 31,</b> |              |
|----------------------------|--------------------------------|--------------|
|                            | <b>2009</b>                    | <b>2008</b>  |
| Other income, net          | \$ 4,268,050                   | \$ 5,287,049 |
| Decrease over prior period | \$ (1,018,999)                 |              |
| Decrease percentage        | (19)%                          |              |

Other income, net, decreased by \$1.0 million, or 19%, to \$4.3 million from \$5.3 million as compared to Fiscal 2008.

The net decrease in other income during Fiscal 2009 when compared to Fiscal 2008 was primarily the result of our recording a profit of \$2.1 million on the sale of certain of our Hover shared hosting assets during Fiscal 2008 as well as our receiving dividends of \$0.5 million during Fiscal 2008 from Afiliias, a company in which we held an investment. Afiliias did not pay any dividends during Fiscal 2009. Effective September 2009, we completed the sale of our investment in Afiliias back to Afiliias and no longer hold any interest in the Company.

This net decrease in other income was partially offset by our recording an incremental gain on the sale of our investment in Afiliias of \$0.8 million during Fiscal 2009 when compared to Fiscal 2008.

In addition, in June 2009 we received an additional payment of \$0.6 million in connection with the Infonautics patents that we assigned in 2002 to a third party. In connection with the assignment of these patents, we retained the right to share in certain revenue relating to any cash flow received by the third party with respect to the commercialization of these patents. This revenue is comparable to

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the \$0.2 million we recognized in June 2008 in connection with these patents. As the third party's costs of commercializing the patents are expected to increase in the future, we do not expect any future revenue received to be material. Also, net interest expense decreased during Fiscal 2009 when compared to the Fiscal 2008 by \$0.4 million, primarily as a result of the monthly capital repayments of \$0.2 million and the annual cash sweep payment of \$0.7 million we made in April 2009 pursuant to the terms of our Bank of Montreal credit facility.

**INCOME TAXES**

The following table presents our provision for income taxes for the periods presented:

|  | Year ended December 31, |            |
|--|-------------------------|------------|
|  | 2009                    | 2008       |
| Provision for (recovery of) income taxes | \$ (251,384)            | \$ 121,134 |

Our provision for income taxes primarily relates to tax on current year taxable income of \$0.5 million; tax expense of \$0.1 million related to revisions to prior year estimates; a benefit of \$0.6 million related to a reduction in the Company's recorded deferred tax liability and a benefit of (\$0.3 million) related to investment tax credits earned during the period. The reduction in the deferred tax liability relates to the rate at which the Company expects the temporary differences resulting from its unlimited life intangibles to reverse. This change in estimate arose as a result of the Company no longer being subject to material state tax in the United States given the change in the jurisdictions in which the Company now operates. We operate in various tax jurisdictions, and accordingly, our income is subject to varying rates of tax. Losses incurred in one jurisdiction cannot be used to offset income taxes payable in another period. Our ability to use income tax loss carryforwards and future income tax deductions is dependent upon our operations in the tax jurisdictions in which such losses or deductions arise.

Our 2008 provision for income taxes primarily relates to our estimate for federal alternative minimum tax obligations for Fiscal 2008 and Pennsylvania state franchise tax related to prior years. No provision for income taxes other than for alternative minimum tax and Pennsylvania franchise tax was recorded during the year because we had net operating losses to offset against our operating income in our major operating jurisdictions. We operate in various tax jurisdictions, and accordingly, our income is subject to varying rates of tax.

Tucows has approximately \$0.1 million of total gross unrecognized tax benefit as of December 31, 2009 and \$0.3 million of total gross unrecognized tax benefit as of December 31, 2008, which if recognized would favorably affect the income tax rate in future periods. The unrecognized tax benefit relates to prior year Pennsylvania state franchise taxes and other US state taxes. The unrecognized tax benefit for the 2009 research and development claim is not expected to be significant. We recognize accrued interest and penalties related to taxes in tax expense. We did not have significant interest and penalties accrued as of December 31, 2009 and December 31, 2008 respectively. We believe it is reasonably possible that \$0.1 million of the unrecognized tax benefit will decrease in the next twelve months as it is anticipated that the U.S. tax authorities will finalize their review of prior taxes owing in Pennsylvania within the period and certain other prior year state tax returns will be filed.

A reconciliation of the federal statutory income tax rate to our effective tax rate is set forth in Note 11 of Notes to Consolidated Financial Statements included in this Form 10-K.

***Liquidity and capital resources***

As of December 31, 2010, our cash and cash equivalents balance decreased by \$5.4 million to \$4.2 million, from \$9.6 million as at December 31, 2009. This decrease in cash is attributable to the success we have experienced with our share repurchase programs during Fiscal 2010. Our principal

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source of liquidity during Fiscal 2010 was net cash provided by operating activities. Fluctuations in foreign exchange rates had a material impact on the balances of our assets and liabilities year-over-year as reported in our consolidated balance sheets, which impacted amounts shown in our consolidated statement of cash flows.

We have credit agreements with the Bank of Montreal that provides us access to:

1. a non-revolving, reducing demand loan facility that was used to fund the acquisition of Innerwise, Inc. during 2007 under which \$1.3 million was owing as of December 31, 2010. Based on the anticipated annual cash sweep payment for Fiscal 2010, we expect that this remaining balance will be fully repaid by June 2011;
2. a non-revolving, reducing demand loan facility for \$2.0 million which can be used to finance the repurchase of our common shares. As of December 31, 2010, we had no borrowings under this credit facility;
3. an operating demand loan for \$1.0 million to fund operational requirements. As of December 31, 2010, we had no borrowings under this credit facility; and
4. a Treasury Risk Management Facility for \$3.5 million to be used as a line to fund any settlement risk exposure that may arise from foreign exchange contracts we enter into from time to time to mitigate the exchange rate risk on portions of our Canadian dollar exposure. At December 31, 2010, we had forward exchange contracts to trade \$15.9 million U.S. dollars in exchange for Canadian dollars.

Our credit agreement contains customary representations and warranties, affirmative and negative covenants, and events of default. Our credit agreement also requires us to make annual cash sweep payments on our non-revolving, reducing demand loans. They also require us to comply with certain customary non-financial covenants as well as certain financial covenants. As of and for the year ended December 31, 2010, we were in compliance with these covenants.

Net cash provided by operating activities for Fiscal 2010 totaled \$6.8 million, compared to \$6.5 million for Fiscal 2009. Net cash provided by operating activities, before changes in non-cash operating working capital decreased by \$0.6 million to \$6.9 million for Fiscal 2010 compared to \$7.5 million for Fiscal 2009 primarily the result of the impact of the strengthening Canadian dollar on our results. Net cash used in non-cash operating working capital decreased by \$0.9 million to \$0.1 million for Fiscal 2010 compared to \$1.0 million for Fiscal 2009.

This improvement in non-cash operating working capital was primarily the result of deferred revenue net or prepaid domain name registry and other Internet service fees increasing by \$0.7 million compared to Fiscal 2009. In addition, reductions of \$1.2 million in deposits we maintain with our registry suppliers and income taxes recoverable during Fiscal 2010 as compared to Fiscal 2009 were partially offset by an increase in accounts receivable of \$0.6 million and a decrease in accounts payable and accruals of \$0.4 million as compared to Fiscal 2009.

Net cash used in financing activities during Fiscal 2010 totaled \$11.6 million as compared to \$5.5 million used during Fiscal 2009. Of this \$11.6 million, \$9.7 million was used to fund share repurchases and \$1.9 million was used for principal repayments under our non-revolving, reducing demand loan facility.

Under our share repurchase programs we used \$7.3 million to repurchase 10.3 million of our shares pursuant to the terms of two Dutch auction tender offers completed during January 2010 and October 2010, and \$2.4 million to repurchase 3.4 million of our shares under the terms of our stock repurchase program announced in February 2010. These initiatives have resulted in a 20% reduction in our issued and outstanding shares as compared to our issued and outstanding shares at December 31, 2009.

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Investing activities used net cash of \$0.6 million to acquire additional property and equipment during Fiscal 2010, as compared to the \$3.3 million in cash provided by investing activities during Fiscal 2009. This generation of cash during Fiscal 2009 resulted from our receipt of \$4.1 million in proceeds from the disposition of our investment in Afiliac, which was partially offset by \$0.8 million invested to acquire additional property and equipment during Fiscal 2009.

Based on our operations, we believe that our cash flow from operations will be adequate to meet our anticipated requirements for working capital, capital expenditures and loan repayments for at least the next 12 months.

We may choose to raise additional funds or seek other financing arrangements to facilitate more rapid expansion, develop new or enhance existing products or services, respond to competitive pressures or acquire or invest in complementary businesses, technologies, services or products.

If additional financing is required, we may not be able to raise it on acceptable terms, or at all, and additional financing may be dilutive to existing investors. We may also evaluate potential acquisitions of other businesses, products and technologies. To complete potential acquisitions, we may issue additional securities or need additional equity or debt financing and any additional financing may be dilutive to existing investors. There are currently no material understandings, commitments or agreements regarding the acquisition of other businesses.

**Subsequent events**

In March 2011 we received notification that we have earned an additional amount of \$0.3 million as a result of a routine audit in connection with Infonautics patents that we assigned in 2002 to a third party who continues to commercialize these patents. We expect payment of this amount imminently. In connection with the assignment of these patents, we retained the right to share in certain revenue relating to any cash flow received by such third party. This revenue is comparable to the \$0.6 million we recognized in June 2009 in connection with these patents. As the costs of commercializing the patents are expected to increase in the future, we do not expect any future revenue received to be material.

**Off Balance Sheet Arrangements and Contractual Obligations**

We have not entered into any off balance sheet financial arrangements and have not established any special purpose entities as of December 31, 2010 nor have we guaranteed any debt or commitment of other entities. As such, we are not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Our sales are primarily made in U.S. dollars, while a major portion of expenses are incurred in Canadian dollars. Our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. Our interest income is sensitive to changes in the general level of Canadian and U.S. interest rates, particularly since the majority of our investments are in short-term instruments. Based on the nature of our short-term investments, we have concluded that there is no material interest rate risk exposure at December 31, 2010.

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Although we have a functional currency of U.S. dollars, a major portion of our fixed expenses are incurred in Canadian dollars. Our policy with respect to foreign currency exposure is to manage financial exposure to certain foreign exchange fluctuations with the objective of neutralizing some of the impact of foreign currency exchange movements. Accordingly, we have entered into numerous foreign exchange contracts to mitigate the exchange rate risk on portions of our Canadian dollar exposure. The following contracts were entered into in 2010 in order to manage our exposure to foreign exchange rate fluctuations:

On January 20, 2010, we entered into a series of forward foreign exchange contracts, whereby amounts of \$650,000 are converted into Canadian dollars on a semi-monthly basis from May 2010 to July 2010 at foreign exchange rates ranging from 1.0300 to 1.0375.

On February 25, 2010, we entered into a series of forward foreign exchange contracts, whereby amounts of \$650,000 are converted into Canadian dollars on a semi-monthly basis from July 2010 to August 2010 at foreign exchange rates ranging from 1.0604 to 1.0609.

On March 24, 2010, we entered into a series of forward foreign exchange contracts, whereby amounts of \$650,000 are converted into Canadian dollars on a semi-monthly basis in September 2010 at a foreign exchange rate of 1.0180.

On May 6, 2010, we entered into a series of forward foreign exchange contracts, whereby amounts of \$400,000 are converted into Canadian dollars on a semi-monthly basis from October 2010 to November 2010 at a foreign exchange rate of 1.0313.

On May 6, 2010, we entered into a series of forward foreign exchange contracts, whereby amounts of \$250,000 are converted into Canadian dollars on a semi-monthly basis from October 2010 to November 2010 at a foreign exchange rate of 1.0460.

On May 25, 2010, we entered into a series of forward foreign exchange contracts, whereby amounts of \$250,000 are converted into Canadian dollars on a semi-monthly basis from January 2011 to March 2011 at a foreign exchange rate of 1.0732.

As we do not comply with the documentation requirements for hedge accounting, we account for the fair value of the derivative instruments within the consolidated balance sheet as a derivative financial asset or liability and the corresponding change in fair value is recorded in the consolidated statement of operations. We have no other freestanding or embedded derivative instruments.

The impact of the fair value adjustment on unrealized foreign exchange forward contracts for Fiscal 2010 was a net loss of approximately \$1.4 million, and for Fiscal 2009, the impact was a net gain of approximately \$4.2 million, which is reflected on the consolidated statements of operations. As of December 31, 2010, we had outstanding foreign currency forward contracts with a notional value of \$15.9 million. As of December 31, 2009, we had outstanding foreign currency forward contracts with a notional value of \$25.2 million.

We have performed a sensitivity analysis model for foreign exchange exposure over Fiscal 2010. The analysis used a modeling technique that compares the U.S. dollar equivalent of all expenses incurred in Canadian dollars, at the actual exchange rate, to a hypothetical 10% adverse movement in the foreign currency exchange rates against the U.S. dollar, with all other variables held constant. Foreign currency exchange rates used were based on the market rates in effect during Fiscal 2010. The sensitivity analysis indicated that a hypothetical 10% adverse movement in foreign currency exchange rates would result in a decrease in net income for Fiscal 2010 of approximately \$1.5 million. There can be no assurance that the above projected exchange rate decrease will materialize. Fluctuations of exchange rates are beyond the actions to hedge or mitigate these risks.

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**Credit Risk**

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash equivalents, marketable securities, foreign exchange contracts and accounts receivable. Our cash, cash equivalents and short-term investments are in high-quality securities placed with major banks and financial institutions whom we have evaluated as highly creditworthy and commercial paper. Similarly, we enter into our foreign exchange contracts with major banks and financial institutions. With respect to accounts receivable, we perform ongoing evaluations of our customers, generally granting uncollateralized credit terms to our customers, and maintaining an allowance for doubtful accounts based on historical experience and our expectation of future losses.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Our consolidated financial statements and supplementary data required by this item are attached to this Annual Report on Form 10-K beginning on page F-1.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A (T). CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for Tucows. Under the supervision of our Chief Executive Officer and Chief Financial Officer, our management conducted an assessment of the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based on the results of such assessment, management have concluded that our disclosure controls and procedures as of the end of the period covered by this report are effective. There were no changes in our internal control over financial reporting during the quarter ended December 31, 2010 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Internal Control over Financial Reporting.**

There have not been any changes in our internal control over financial reporting during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within Tucows have been detected. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Management's report on internal control over financial reporting is included on page F-2 of this Annual Report on Form 10-K.



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**ITEM 9B. OTHER INFORMATION**

None.

**PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

**Stanley Stern** Chairman of the Board of Directors since August 2001

Mr. Stern, 53, has been a Managing Director and Head of Technology and Financial Institutions Investment Banking with Oppenheimer & Co. Inc., an investment banking firm, since April 2004. From February 2002 to March 2004, Mr. Stern served as a Managing Director and Head of Investment with C.E. Unterberg, Towbin, an investment banking firm. From January 2000 to February 2002, Mr. Stern served as Managing Director of STI Ventures Advisory USA Inc. and as a member of the Board of Directors and the investment committee of STI Ventures, a venture capital company focusing on the high technology market.

Mr. Stern's has extensive experience with technology based companies in the context of his investment banking experience, and has an in-depth knowledge of the Company's business, strategy and management team, all of which qualify him to be a director of Tucows.

**Eugene Fiume** Director since June 2005

Mr. Fiume, 53, is a Professor (since 1995) and past Chair (1998-2004) of the Department of Computer Science at the University of Toronto, where he also co-directs the Dynamic Graphics Project. He is the inaugural director of the Department's new professional master's programme.

Mr. Fiume has held many advisory board roles in both the public and private sectors. He currently works with venture capital companies and SMEs on due diligence, strategy and human resources.

Mr. Fiume has an extensive and evolving knowledge of computer science in the context of his experience as a Professor at the University of Toronto. In addition, he has other valuable experience with technology companies generally that, in addition to the other attributes listed above, qualify him to be a director of Tucows.

**Erez Gissin** Director since August 2001

Mr. Gissin, 52, has served since 2005 as the Chief Executive Officer of BCID Ltd., an investment company focusing on infrastructure development projects in China. From July 2000 to March 2005, Mr. Gissin has served as the Chief Executive Officer of IP Planet Networks Ltd., an Israeli satellite communication operator providing Internet backbone connectivity and solutions to Internet Service Providers. From July 1995 to July 2000, Mr. Gissin was Vice President, Business Development of Eurocom Communications Ltd., a holding company that controls several telecommunications services, equipment and Internet companies in Israel. Mr. Gissin is also a director of Partner Communications Ltd. (NASDAQ: PTNR)

Mr. Gissin has a strong background in the internet communications industry and has gained significant institutional knowledge in his long tenure as one of our directors. Mr. Gissin also has significant leadership experience as the Chief Executive Officer of BCID Ltd. and IP Planet Networks Ltd. and he has extensive financial acumen derived from his years of executive experience. All of these qualities qualify Mr. Gissin to be a director of Tucows.

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**Joichi Ito** Director since December 2008

Mr Ito, 44, is General Manager of Neoteny Labs, a startup fund focusing on Asia and the Middle East. He is also the Chairman of Creative Commons, where has serviced on the board since April 2008, a co-founder of Digital Garage, where he has served on the board since September 2006, as well as a Senior Visiting Researcher of Keio Research Institute at the Shonan Fujisawa Campus of Keio University in Japan. Since December 2003 Mr. Ito has served as the Chairman of Six Apart Japan, a weblog software company.

From June 2002 until July 2008, Mr. Ito served on the board of Pia Corporation, a ticket and entertainment magazine company in Japan (Tokyo Stock Exchange 4337). Since May 2009 Mr. Ito has served on the board of CCC, a video rental franchise company in Japan (Tokyo Stock Exchange 4756). He served on the board of ICANN, a U.S. non-profit corporation, from December 2004 until December 2007. ICANN manages the domain name registration system that Tucows uses for its domain name business and ICANN receives fees from Tucows for domain name registrations.

Mr. Ito is also on the board of directors of a number of non-profit organizations, including The Mozilla Foundation. He has created numerous Internet companies, including PSINet Japan, Digital Garage (Tokyo Stock Exchange 4819) and Infoseek Japan and was an early stage investor in Twitter, Six Apart, Flickr, SocialText, Dopplr, Last.fum, Rupture and Kongregate. He has served and continues to serve on various Japanese central as well as local government committees and boards, advising the government on IT, privacy and computer security related issues.

Mr. Ito has extensive experience as a director of a number of publicly traded companies and has a wide range of experience with internet companies generally. This experience, along with Mr. Ito's domain-specific knowledge, enable him to bring key experience to the Company and qualifies him to be a director of Tucows.

**Allen Karp** Director since October 2005

Mr. Karp, 70, was with Cineplex Odeon Corporation in various positions since 1986, where he retired as Chairman and Chief Executive Officer in 2002 and as Chairman Emeritus in 2005. From 1966 to 1986, he practiced law at the law firm of Goodman and Carr LLP, where he was named partner in 1970. Mr. Karp is a Director of Brookfield Real Estate Services Inc., the Chair of its corporate governance committee and sits on the audit committee. Mr. Karp is Chairman of the board of Directors of IBI Group Inc., and is Chairman of the Nominating, Governance and Compensation Committee. Mr. Karp is a director of the Toronto International Film Festival Group, where he served as Chairman from 1999 to 2007 and has served as Chairman of its corporate governance committee since 2007.

Mr. Karp has extensive executive leadership skills, long-standing senior management experience, a strong ethics and compliance focus and audit committee experience. These skills and qualifications, in addition to his current service on the boards of directors of other public companies, enable him to bring valuable perspectives to our Board, particularly with respect to corporate governance matters, and qualify him to be a director of Tucows.

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**Lloyd Morrisett** Director since February 1994

Dr. Morrisett, 81, served as a director and as a member of the audit committee and compensation committee of Infonautics, Inc., our predecessor, beginning in February 1994. Dr. Morrisett also served as chairman of the Board of Directors of Infonautics beginning in March 1998 until we merged with Tucows Delaware in August 2001 and became Tucows Inc. He is the co-founder of the Children's Television Workshop now Sesame Workshop and served from 1969 to 1998 as president of The Markle Foundation, a charitable organization.

The breadth of Dr. Morrisett's career has provided him with extensive business acumen and leadership experience. In addition, as a member of the board of directors of our predecessor, Dr. Morrisett is uniquely positioned to provide our Board and the Company with an important historical perspective with respect to the Company's operations and strategy. These factors, combined with Dr. Morrisett's experience as a public company board, audit committee and compensation committee member qualify him to be a director of Tucows.

**Elliot Noss** Director since August 2001

Mr. Noss, 48, is our President and Chief Executive Officer and has served in such capacity since the completion of our merger with Tucows Delaware in August 2001. From May 1999 until completion of the merger in August 2001, Mr. Noss served as President and Chief Executive Officer of Tucows Delaware. Before that, from April 1997 to May 1999, Mr. Noss served as Vice President of Corporate Services of Tucows Interactive Ltd., which was acquired by Tucows Delaware in May 1999.

Mr. Noss's lengthy service as our Chief Executive Officer has provided him with extensive knowledge of, and experience with, Tucows' operations, strategy and financial position. In addition, Mr. Noss has widespread knowledge of the internet and software industry generally that, coupled with his operational expertise, qualifies him to be a director of Tucows.

**Rawleigh H. Ralls** Director since May, 2009

Mr. Ralls, 48, is a founding partner of Lacuna, LLC, an investment management company focused on both public and private companies that he formed in October 2006. Prior thereto, from 1999 to 2006, he was Chairman of Netidentity.com, an Internet email and web hosting company, where he led corporate strategy and development until the firm's sale in 2006. Mr. Ralls currently serves on the Board of Directors of a number of companies, including Savoya, LLC, IntraOp Medical, Knowledge Factor, Mocapay, Inc, and SageFire, Inc.

Mr. Ralls has a wealth of industry experience, most notably the experience that he gained through his leadership of Netidentity.com. In addition, Mr. Ralls contributes a unique perspective to the Board's discussions and considerations based on the two decades of investing and portfolio management experience. All of these attributes qualify Mr. Ralls to be a director of Tucows.

**Jeffrey Schwartz** Director since June 2005

Mr. Schwartz, 48, has served as a director of Dorel Industries since 1987 and as Executive Vice President and Chief Financial Officer since 2003. Mr. Schwartz is a graduate of McGill University in Montreal and has a degree in the field of business administration.

Mr. Schwartz has a significant amount of public-company financial expertise, particularly in his executive experience as the chief financial officer of Dorel Industries, Inc. This executive experience, along with Mr. Schwartz's service as one of our audit committee members (and as Chairman of our audit committee since 2005), qualifies him to be a director of Tucows.

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Our directors are elected annually and serve until the election or appointment and qualification of their successors or their earlier death, resignation or removal.

**Executive Officers**

The required information regarding our executive officers is set forth in Part I hereof under the caption "Executive Officers of the Registrant" and is incorporated herein by reference.

**Governance Principals**

The governance principals of our Board of Directors include the charters of our audit committee, our Corporate Governance and Compensation Committee, our Code of Conduct, and our Code of Ethics. Each of these documents and various other documents embodying our governance principals are published on our website at [tucowsinc.com](http://tucowsinc.com). Amendments and waivers of our Code of Ethics will either be posted on our website or filed with the SEC on a current report on Form 8-K.

Mr. Stern, one of our independent directors, serves as the Chairman of the Board. The Board does not have a lead independent director. Our Board currently consists of eight directors, seven of whom the Board has determined are "independent" within the meaning of the independence requirements prescribed by the listing standards of NYSE Amex. The Board believes that this structure, which provides an overwhelming majority of independent directors, coupled with the Board meeting in executive session without any management directors or non-independent directors present, is an appropriate structure for Tucows' Board. We believe that this structure provides the appropriate, independent oversight by the Board. The Board regularly consults with our Chief Executive Officer, who is also a director, and our corporate governance, nominating and compensation committee to review the various types of risk that affect Tucows and the strategies to mitigate such risks. The Board believes that this structure has been effective.

**Meetings**

Our Board of Directors met five times during Fiscal 2010. Our Board of Directors also took action by unanimous written consent on two occasions during Fiscal 2010. Each director attended at least 80% of the total number of meetings of the Board of Directors and the committees on which he served during Fiscal 2010.

**Executive Sessions of Independent Directors**

A majority of the independent directors meet quarterly in executive sessions without members of our management present. Mr. Stern was responsible for chairing the executive sessions.

**Policy regarding attendance**

Directors are expected, but are not required, to attend board meetings, meetings of committees on which they serve, and shareholder meetings, and to spend the time needed and meet as frequently as necessary to discharge their responsibilities properly. Elliot Noss attended our 2010 annual meeting of shareholders in person while the remainder of the Board of Directors attended by teleconference.

**Committees**

Our Board of Directors has two committees, an audit committee established in accordance with Section 3(a)(58)(A) of the Securities Exchange Act of 1934, as amended, and a corporate governance, nomination and compensation committee. The Board of Directors created the corporate governance, nomination and compensation committee and adopted a new charter in November 2007 in order to expand the responsibilities of our compensation committee to include oversight of our corporate

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governance principles and our Board nomination process. Our committees generally meet in connection with regularly scheduled quarterly and annual meetings of the Board of Directors, with additional meetings held as often as its members deem necessary to perform its responsibilities. From time to time, depending on the circumstances, the board may form a new committee or disband a current committee.

*The audit committee* currently consists of Mr. Schwartz, Mr. Karp and Dr. Morrisett, all of whom are independent directors as defined in Section 121A of the NYSE Amex listing standards.

The audit committee held five meetings during Fiscal 2010. The audit committee also took action by unanimous written consent on one occasion during the 2010 fiscal year. The audit committee's purposes are:

- To assist the Board of Directors in its oversight of (1) our accounting and financial reporting processes and the audits of our financial statements, and (2) our compliance with legal and regulatory requirements;
- To interact directly with and evaluate the performance of the independent auditors, including to determine whether to engage or dismiss the independent auditors and to monitor the independent auditors' qualifications and independence; and
- To prepare the report required by the rules of the SEC to be included in our annual Form 10-K.

Each of the members of our audit committee is an independent director and satisfies the independence standards specified in Section 121A of the NYSE Amex listing requirements and Rule 10A-3 under the Securities Exchange Act of 1934, and is able to read and understand fundamental financial statements, including balance sheets, income statements and cash flow statements. Additionally, the Board of Directors has determined that Mr. Schwartz qualifies as an "audit committee financial expert" as defined under Item 407(d)(5) of Regulation S-K. The Board of Directors has adopted a written charter for the audit committee, which the audit committee has reviewed and determined to be in compliance with the rules set forth in the NYSE Amex listing requirements.

*The corporate governance, nomination and compensation committee* currently consists of Mr. Stern, Mr. Schwartz, Dr. Morrisett and Mr. Karp, all of whom are independent directors as defined in Section 121A of the NYSE Amex listing standards.

The responsibilities of this committee include corporate governance and nomination responsibilities. This committee has adopted a formal charter, which is available on [tucowsinc.com](http://tucowsinc.com).

The committee held three meetings during Fiscal 2010. The corporate governance, nomination and compensation committee also took action by unanimous written consent on two occasions during the 2010 fiscal year. The corporate governance, nomination and compensation committee has responsibility for the oversight, review and approval of senior management's compensation philosophy and practices. To assist it in meeting this mandate the corporate governance, nomination and compensation committee has the authority to hire its own independent advisors and is authorized to delegate responsibilities to management, independent accountants and internal and outside lawyers.

The corporate governance, nomination and compensation committee makes recommendations to the Board of Directors on compensation for the chief executive officer and approves the compensation for individuals that report directly to the chief executive officer, including the named executive officers, to ensure that they meet corporate objectives. For this purpose, named executive officers are defined as the chief executive officer, the chief financial officer and our three other most highly compensated executive officers. The Board of Directors and the corporate governance, nomination and compensation committee also review, approve and evaluate short-term and long-term incentive designs and incentive awards for our senior management. The board as a whole reviews the recommendations of the

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corporate governance, nomination and compensation committee and gives final approval on the compensation for the chief executive officer.

This committee is also responsible for recommending qualified candidates to the Board for election as directors, including the slate of directors that the Board proposes for election by stockholders at our Annual Meetings of Shareholder. While the committee does not have a formal diversity "policy," the committee recommends candidates based upon many factors, including diversity of viewpoint and industry, and also seeks to recommend members from diverse backgrounds so that the Board consists of members with a broad spectrum of experience and expertise and with a reputation for integrity. We believe that the committee's existing nominations process is designed to identify the best possible nominees for the Board, regardless of the nominee's gender, racial background, religion, or ethnicity. The committee identifies candidates through a variety of means, including recommendations from members of the Board and suggestions from our management. In addition, the committee considers candidates recommended by third parties, including shareholders, in accordance with the procedures set forth below. The committee will examine each director nominee on a case-by-case basis, regardless of who recommended the nominee, and take into account all factors it considers appropriate, which may include strength of character, mature judgment, career specialization, relevant technical skills or financial acumen, diversity of viewpoint and industry knowledge. However, the Board and the committee believe the following minimum qualifications must be met by a director nominee to be recommended by the committee:

Each director must display high personal and professional ethics, integrity and values.

Each director must have the ability to exercise sound business judgment.

Each director must be accomplished in his or her respective field, with broad experience at the executive and/or policy-making level in business, government, education, technology or public interest.

Each director must have relevant expertise and experience, and be able to offer advice and guidance based on that expertise and experience.

Each director must be able to represent all shareholders of Tucows and be committed to enhancing long-term shareholder value.

Each director must have sufficient time available to devote to activities of the Board and to enhance his or her knowledge of Tucows' business.

**Shareholder nominations to the Board**

Our Board of Directors will consider any candidate proposed in good faith by any of our shareholders that is made in accordance with a resolution adopted by the Board that requires a shareholder to timely submit, to the attention of our Secretary at 96 Mowat Avenue, Toronto, Ontario M6K 3M1 Canada, the following:

the candidate's name and the information about the individual that would be required to be included in a proxy statement under the rules of the SEC;

information about the relationship between the candidate and the nominating shareholder;

the consent of the candidate to serve as a director; and

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proof of the number of our common stock that the nominating shareholder owns and the length of time the shares have been owned.

In order to be considered by the Board of Directors, a shareholder's nomination must be delivered to our secretary at least 120 days before the date on which we first mailed our proxy materials for our

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prior year's annual meeting of shareholders. Subject to compliance with statutory or regulatory requirements, our Board of Directors does not expect that candidates recommended by shareholders will be evaluated in a different manner than other candidates.

**Ethics policy for senior officers**

Our Board of Directors has adopted an ethics policy for our senior officers, including our Chief Executive Officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. A copy of the ethics policy for senior officers can be obtained from our Internet web site at *tucowsinc.com*, without charge.

**Communications with the Board of Directors**

We provide an informal process for shareholders to send communications to our Board of Directors. If you wish to communicate with our Board of Directors, you may send correspondence to the attention of our Secretary at 96 Mowat Avenue, Toronto, Ontario M6K 3M1 Canada. The Secretary will submit your correspondence to the chairman of the Board of Directors, the chairman of the appropriate committee, or the appropriate individual director, as applicable.

**Director compensation**

Directors who are employees receive no additional or special compensation for serving as directors. The Board of Directors determines the total amount of the annual retainer as well as the amounts of any meeting or committee fee based upon recommendations from the corporate governance, nomination and compensation committee of the board and input from the chief executive officer.

**Equity compensation**

Under the terms of our 2006 Amended and Restated Equity Compensation Plan (the "2006 Plan"), we make automatic formula grants of nonqualified stock options to our non-employee directors and members of committees of our Board of Directors as described below. All stock-based compensation for our Non-employee directors is governed by the 2006 Plan or its predecessor, our 1996 Equity Compensation Plan (the "1996 Plan"). All options granted under the automatic formula grants are immediately exercisable, have an exercise price equal to the fair market value per 2006 terminated by the per share price as of the close of business on the date of grant and have a five-year term. Options are granted to directors under the 2006 Plan as follows:

on the date each non-employee director becomes a director, he or she is granted options to purchase 25,000 shares of our common stock;

on the date each director becomes a member of the audit committee, he or she is granted options to purchase 20,000 shares of our common stock;

on the date each director becomes a member of the corporate governance, nomination and compensation committee, he or she is granted options to purchase 15,000 shares of our common stock;

on each date on which we hold our annual meeting of shareholders, each non-employee director in office immediately before and after the annual election of directors will receive an automatic grant of options to purchase 20,000 of our common stock;

on each date on which we hold our annual meeting of shareholders, each member of the audit committee in office immediately before and after the annual election of directors will receive an automatic grant of options to purchase 10,000 of our common stock; and





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on each date on which we hold our annual meeting of shareholders, each member of the corporate governance, nomination and compensation committee in office immediately before and after the annual election of directors will receive an automatic grant of options to purchase 7,500 shares of our common stock.

**Non-Equity compensation**

The chairman of our Board receives an annual fee of \$10,000, non-employee directors receive an additional annual fee of \$10,000, non-employee directors who serve as members of our audit committee receive an additional annual fee of \$8,000 and non-employee directors who serve on our corporate governance, nomination and compensation committee, receive an annual fee of \$8,000. In addition, all non-employee directors receive the following meeting attendance fees:

**Director meeting attendance fees:**

|  |          |
|--|----------|
| Board Meeting Personal Attendance Fees (per meeting)   | \$ 3,000 |
| Regularly Scheduled Telephonic Board Meeting Attendance Fees (per meeting)   | \$ 500   |
| Regularly Scheduled Telephonic Audit Committee Meeting Attendance Fees (per meeting)   | \$ 250   |
| Regularly Scheduled Telephonic Corporate Governance, Nomination and Compensation Committee Meeting Attendance Fees (per meeting) | \$ 250   |

All fees paid to directors are paid in quarterly installments.

We also purchase directors and officer's liability insurance for the benefit of our directors and officers as a group in the amount of \$10 million. We also reimburse our directors for their reasonable out-of-pocket expenses incurred in attending meetings of our Board of Directors or its committees. No fees are payable to directors for attendance at specially called meetings of the board.

The table below shows all compensation paid to each of our non-employee directors during 2010. Each of the directors listed below served for the entire year.

| Name             | Fees earned or paid in cash (\$) | Option awards (\$)(1)(2) | All other compensation (\$) | Total (\$) |
|------------------|----------------------------------|--------------------------|-----------------------------|------------|
| (a)              | (b)                              | (d)                      | (g)                         | (h)        |
| Stanley Stern    | 36,000                           | 17,008                   |                             | 53,008     |
| Eugene Fiume     | 17,500                           | 6,060                    |                             | 23,560     |
| Erez Gissin      | 17,500                           | 13,000                   |                             | 30,500     |
| Joichi Ito       | 17,000                           | 6,060                    |                             | 23,060     |
| Allen Karp       | 35,000                           | 11,363                   |                             | 46,363     |
| Lloyd Morrisett  | 35,000                           | 18,303                   |                             | 53,303     |
| Rawleigh Ralls   | 14,000                           | 6,060                    |                             | 20,060     |
| Jeffrey Schwartz | 35,000                           | 11,363                   |                             | 46,363     |
|                  | 207,000                          | 89,217                   |                             | 296,217    |

(1)

On May 17, 2010 under the 2006 Plan, Erez Gissin and Lloyd Morrisett were each awarded 20,000 incremental options, and Stanley Stern was awarded 25,000 incremental options. Under the 2006 Plan these options vested immediately and carry an exercise price of \$0.70. All these options remained outstanding at December 31, 2010 and have a five year term. The aggregate grant date fair value of the option grants was determined in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification Topic 718 ("FASB ASC 718"), (formerly Statement of Financial Accounting Standards No. 123(R)) and based on the Black-Scholes option-pricing model and used the same assumptions that are set forth in Note 10 to

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our audited consolidated financial statements included elsewhere in this Annual Report on Form 10-K.

(2)

On September 7, 2010 under the 2006 Plan, our non-employee directors were awarded these automatic formula option grants. Under the 2006 Plan, these options vested immediately and carry an exercise price of \$0.62. All these options remained outstanding at December 31, 2010 and have a five year term. The aggregate grant date fair value of the option grants was calculated in accordance with FASB ASC 718 and based on the Black-Scholes option-pricing model and used the same assumptions that are set forth in Note 10 to our audited consolidated financial statements included in this annual report on Form 10-K for the fiscal year ended December 31, 2010.

**SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our directors and executive officers and persons who own more than 10 percent of a registered class of our equity securities to file with the SEC reports of ownership and reports of changes in ownership of our common stock and our other equity securities. These persons are required by SEC regulation to furnish us with copies of all Section 16(a) reports they file.

We believe that, under the SEC's rules and based solely upon our review of the copies of the Forms 3, 4 and 5 furnished to us, or written representations from certain reporting persons that any such Forms have been filed in a timely manner and that all of our executive officers, directors and persons who own more than 10 percent of a registered class of our equity securities complied with all Section 16(a) filing requirements applicable to them during 2010.

**Stock ownership of management**

We encourage stock ownership by our directors, officers and employees to align their interests with your interests as shareholders. Under Section 16(a) of the Securities and Exchange Act of 1934, as amended, directors, officers and certain beneficial owners of the Company's equity securities are required to file reports of their transactions in the Company's equity securities with the Securities and Exchange Commission on specified due dates. With respect to Fiscal 2010, reports of transactions by all directors, officers and such beneficial holders were timely filed. In making this statement, the Company has relied on the written representations of its directors, officers and holders of more than ten percent (10%) of our outstanding common stock as reported in their filings with the Securities and Exchange Commission.

Table of Contents**ITEM 11. EXECUTIVE COMPENSATION****Summary compensation table**

The following Summary Compensation table provides a summary of the compensation earned by the chief executive officer, Elliot Noss, and our two other most highly compensated executive officers for services rendered in all capacities during 2010. Specific aspects of this compensation are dealt with in further detail in the tables that follow. All dollar amounts below are shown in U.S. dollars. If necessary, amounts that were paid in Canadian dollars during the 2010 fiscal year were converted into U.S. dollars based upon the exchange rate of 1.0367 Canadian dollars for each U.S. dollar, which represents the average Bank of Canada exchange rate for 2010.

| Name and Principal Position           | Year | Salary (\$) | Bonus(1) (\$) | Stock Awards(2) (\$) | Option Awards(3) (\$) | All Other Compensation(4) (\$) | Total (\$) |
|---------------------------------------|------|-------------|---------------|----------------------|-----------------------|--------------------------------|------------|
| (a)                                   | (b)  | (c)         | (d)           | (e)                  | (f)                   | (i)                            | (j)        |
| Elliot Noss                           | 2010 | 319,041     | 83,270        |                      | 51,584                | 10,128                         | 464,023    |
| President and Chief Executive Officer | 2009 | 275,615     | 74,933        | 32                   |                       | 8,530                          | 359,110    |
| Michael Cooperman                     | 2010 | 249,911     | 57,427        |                      | 51,584                | 11,865                         | 370,787    |
| Chief Financial Officer               | 2009 | 215,898     | 51,678        | 32                   |                       | 8,574                          | 276,182    |
| David Woroch                          | 2010 | 207,377     | 57,427        |                      | 51,584                | 7,235                          | 323,623    |
| Vice President, Sales                 | 2009 | 179,150     | 51,678        | 32                   |                       | 6,124                          | 236,984    |

(1)

Represents bonus earned during the fiscal years ended December 31, 2010, 2009 and 2008.

Of the 2010 amount, the following amounts will be paid in 2011:

|                   |           |
|-------------------|-----------|
| Elliot Noss       | \$ 25,443 |
| Michael Cooperman | \$ 17,547 |
| David Woroch      | \$ 17,547 |

Of the 2009 amount, the following amounts were paid in February 2010:

|                   |           |
|-------------------|-----------|
| Elliot Noss       | \$ 52,952 |
| Michael Cooperman | \$ 36,519 |
| David Woroch      | \$ 36,519 |

(2)

Represents the aggregate grant date fair value of such awards, calculated in accordance with FASB ASC 718. Please see Note 10 entitled "Stock Options" in the notes to our audited financial statements below, for a discussion of the assumptions underlying these calculations.

(3)

Represents the aggregate grant date fair value of such awards, calculated in accordance with FASB ASC 718. Please see Note 10 entitled "Stock Options" in the notes to our audited financial statements below, for a discussion of the assumptions underlying these calculations.

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(4)

Amounts reported in this column are comprised of the following items:

|                          | Year | Additional<br>Health<br>Spending<br>Credits<br>(\$) | Car<br>Allowance<br>(\$) | Health<br>Club<br>Membership<br>(\$) | All Other<br>Compensation<br>(\$) |
|--------------------------|------|---|--------------------------|--------------------------------------|-----------------------------------|
| <i>Elliot Noss</i>       | 2010 | 1,447   | 8,681                    |                                      | 10,128                            |
|                          | 2009 | 1,312   | 7,218                    |                                      | 8,530                             |
| <i>Michael Cooperman</i> | 2010 | 1,447   | 8,103                    | 2,315                                | 11,865                            |
|                          | 2009 | 1,312   | 6,737                    | 525                                  | 8,574                             |
| <i>David Woroch</i>      | 2010 | 1,447   | 5,788                    |                                      | 7,235                             |
|                          | 2009 | 1,312   | 4,812                    |                                      | 6,124                             |

**Outstanding Equity Awards at Fiscal Year-End**

The following table sets forth information concerning stock options held by the named executive officers as of December 31, 2010:

| Name and Principal Position | Number of<br>Securities<br>Underlying<br>Unexercised<br>Options<br>(#) Exercisable | Number of<br>Securities<br>Underlying<br>Unexercised<br>Options<br>(#) Unexercisable | Option<br>Exercise<br>Price (\$) | Option<br>Expiration<br>Date |
|-----------------------------|--|--|----------------------------------|------------------------------|
| <i>Elliot Noss</i>          | 60,000   |  | 0.44                             | 7/1/12                       |
|                             | 214,575  |  | 0.37                             | 8/5/13                       |
|                             | 223,991  |  | 0.37                             | 8/5/13                       |
|                             | 1,394,738  |  | 0.37                             | 8/5/13                       |
|                             | 76,500   |  | 0.36                             | 8/4/13                       |
|                             | 200,000  |  | 0.58                             | 8/10/14                      |
|                             | 112,500  | 37,500   | 0.85                             | 3/18/14                      |
|                             | 30,000   | 30,000   | 0.60                             | 5/22/15                      |
|                             |  | 128,000  | 0.70                             | 5/16/17                      |
|                             | 2,312,304  | 195,500  |                                  |                              |
| <i>Michael Cooperman</i>    | 50,000   |  | 0.44                             | 7/1/12                       |
|                             | 629,975  |  | 0.37                             | 8/5/13                       |
|                             | 76,500   |  | 0.36                             | 8/4/13                       |
|                             | 150,000  |  | 0.58                             | 8/10/14                      |
|                             | 90,000   | 30,000   | 0.85                             | 3/18/14                      |
|                             | 37,500   | 37,500   | 0.60                             | 5/22/15                      |
|                             |  | 128,000  | 0.70                             | 5/16/17                      |
|                             | 1,033,975  | 195,500  |                                  |                              |
| <i>David Woroch</i>         | 42,915   |  | 0.49                             | 6/30/12                      |
|                             | 20,000   |  | 0.44                             | 7/1/12                       |
|                             | 30,000   |  | 0.36                             | 8/4/13                       |
|                             | 60,000   |  | 0.58                             | 8/10/14                      |
|                             | 60,000   | 20,000   | 0.85                             | 3/18/14                      |
|                             | 32,500   | 32,500   | 0.60                             | 5/22/15                      |
|                             |  | 128,000  | 0.70                             | 5/16/17                      |
|                             | 245,415  | 180,500  |                                  |                              |

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The stock options grants listed in the above table were issued under our 1996 Plan as well as under our 2006 Plan.

Under the 1996 Plan, these options vest over a period of four years and have a 10 year term. These options are not exercisable for one year after the grant. Thereafter they become exercisable at the rate of 25% after the first year, with the remaining 75% vesting evenly at each month end over the next thirty six months, becoming fully exercisable after the fourth year.

Under the 2006 Plan, these options vest over a period of four years and have a 7 year term. These options are not exercisable for one year after the grant. Thereafter they become exercisable at the rate of 25% per annum, becoming fully exercisable after the fourth year.

**Potential Payments on Termination or Change In Control**

We have certain agreements that require us to provide compensation to our named executive officers in the event of a termination of employment or a change in control of Tucows. These agreements are summarized following the table below and do not include any payment for termination for cause. The tables below show estimated compensation payable to each named executive officer upon various triggering events. Actual amounts can only be determined upon the triggering event.

| Elliot Noss(1)                            | 2010 | Termination<br>without Cause | Change in<br>Control |
|---|------|------------------------------|----------------------|
| <b>Compensation</b>                       |      |                              |                      |
| Base Salary/Severance(2)                  |      | \$ 638,082                   | \$ 1,126,082         |
| Bonus Plan(3)                             |      | 308,407                      | 308,407              |
| Acceleration of Unvested Equity Awards(4) |      | 7,740                        | 7,740                |
| <b>Benefits(5)</b>                        |      |                              |                      |
| Car Allowance                             |      | 8,681                        | 8,681                |
| Healthcare Flexible Spending Account      |      | 1,447                        | 1,447                |
| Healthclub                                |      |                              |                      |
|   |      | \$ 964,357                   | \$ 1,452,357         |

| Michael Cooperman(1)                      | 2010 | Termination<br>without Cause | Change in<br>Control |
|---|------|------------------------------|----------------------|
| <b>Compensation</b>                       |      |                              |                      |
| Base Salary/Severance(2)                  |      | \$ 333,215                   | \$ 577,215           |
| Bonus Plan(3)                             |      | 141,796                      | 141,796              |
| Acceleration of Unvested Equity Awards(4) |      | 3,001                        | 8,715                |
| <b>Benefits(5)</b>                        |      |                              |                      |
| Car Allowance                             |      | 8,103                        | 8,103                |
| Healthcare Flexible Spending Account      |      | 1,447                        | 1,447                |
| Healthclub                                |      | 2,315                        | 2,315                |
|   |      | \$ 489,877                   | \$ 739,591           |

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| David Woroch(1)                           | 2010 | Termination<br>without Cause | Change in<br>Control |
|---|------|------------------------------|----------------------|
| <b>Compensation</b>                       |      |                              |                      |
| Base Salary/Severance(2)                  |      | \$ 259,222                   | \$ 259,222           |
| Bonus Plan(3)                             |      | 132,934                      | 132,934              |
| Acceleration of Unvested Equity Awards(4) |      | 2,601                        | 2,601                |
| <b>Benefits(5)</b>                        |      |                              |                      |
| Car Allowance                             |      | 5,788                        | 5,788                |
| Healthcare Flexible Spending Account      |      | 1,447                        | 1,447                |
| Healthclub                                |      |                              |                      |
|   |      | \$ 401,992                   | \$ 401,992           |

- (1) For the purpose of the table we assumed an annual base salary at the executive's level as of December 31, 2010
- (2) Severance for Mr. Noss is compensation for one year plus one month additional compensation for each completed year of service capped at 24 months. For Messrs. Cooperman and Woroch, severance compensation is for six months plus one month additional compensation for each completed year of service.
- (3) For the purpose of the table we assumed that the annual incentive bonus target as of December 31, 2010 had been achieved and that no overachievement bonus or special bonuses would be payable.
- (4) For purposes of the above table, we have assumed that if we terminate Mr. Noss without cause all his unvested options vest automatically and that for Messrs. Cooperman or Woroch, that their options continue to vest through any severance period. On a change in control we have assumed that all unvested options for Messrs. Noss or Cooperman vest automatically and that for Mr. Woroch, that his options continue to vest through and until the end of any severance period. Amounts disclosed in this table equal the closing market value of our common stock as of December 31, 2010, minus the exercise price, multiplied by the number of unvested shares of our common stock that would vest. The closing market value of our common stock on December 31, 2010 was \$0.73.
- (5) Pay for unused vacation, extended health, matching registered retirement savings plan benefit, life insurance and accidental death and dismemberment insurance are standard programs offered to all employees and are therefore not reported.

**Employment Agreements Termination**

Employment contracts are currently in place for each of the named executive officers, whose contracts detail the severance payments that will be provided on termination of employment and the consequent obligations of non-competition and non-solicitation.

The following details the cash severance payment that will be paid to each of the named executive officers in the event of termination without cause or termination for good reason.

Upon termination without cause, Mr. Woroch is entitled to a severance payment in the amount of six months' compensation plus one months' compensation for each additional completed year of service. Severance payments can be made in equal monthly installments. Mr. Woroch is bound by a standard non-competition covenant for a period of twelve months following their termination.

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Messrs Noss and Cooperman's employment agreements are subject to early termination by us due to:

the death or disability of the executive;

for "cause;" or

without "cause."

If we terminate Mr. Noss without "cause," he is entitled to receive 12 months of compensation plus one month of compensation for each year of service, to a maximum of 18 months of compensation.

If we terminate Mr. Cooperman's employment without "cause," he is entitled to receive six months of compensation plus one month of compensation for each year of service.

For purposes of the employment agreements, "cause" is defined to mean the executive's conviction (or plea of guilty or nolo contendere) for committing an act of fraud, embezzlement, theft or other act constituting a felony or willful failure or an executive's refusal to perform the duties and responsibilities of his position, which failure or refusal is not cured within 30 days of receiving a written notice thereof from our Board of Directors.

***Employment Agreements Change in Control***

Under their employment agreements, both Mr. Noss and Mr. Cooperman are also entitled to the change in control benefits described in the following paragraph if:

the executive resigns with or without "good reason" within the 30-day period immediately following the date that is six months after the effective date of the "change in control;" or

within 18 months after a "change in control" and executive's employment is terminated either:

without "cause;" or

by resignation for "good reason."

If an executive's employment is terminated following a change in control under the circumstances described in the preceding paragraph, the executive is entitled to receive a lump sum payment based upon the fair market value of the Company on the effective date of the "change in control" as determined by our Board of Directors in the exercise of good faith and reasonable judgment taking into account, among other things, the nature of the "change in control" and the amount and type of consideration, if any, paid in connection with the "change in control." Depending on the fair market value of the company, the lump sum payments range from \$375,000 to \$2 million in the case of Mr. Noss, and from \$187,500 to \$1 million in the case of Mr. Cooperman. In addition to the lump sum payments, all stock options held by the executive officers will be immediately and fully vested and exercisable as of the date of termination.

A "change in control" is generally defined as:

the acquisition of 50% or more of our common stock;

a change in the majority of our Board of Directors unless approved by the incumbent directors (other than as a result of a contested election); and



certain reorganizations, mergers, consolidations, liquidations, or dissolutions, unless certain requirements are met regarding continuing ownership of our outstanding common stock.

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"Good reason" is defined to include the occurrence of one or more of the following:

the executive's position, management responsibilities or working conditions are diminished from those in effect immediately prior to the change in control, or he is assigned duties inconsistent with his position;

the executive is required to be based at a location in excess of 30 miles from his principal job location or office immediately prior to the change in control;

the executive's base compensation is reduced, or the executive's compensation and benefits taken as a whole are materially reduced, from those in effect immediately prior to the change in control; or

we fail to obtain a satisfactory agreement from any successor to assume and agree to perform our obligations to the executive under his employment agreement.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table sets forth the beneficial ownership of our common stock, as of March 18, 2011, by each of our chief executive officer, our two other most highly compensated executive officers, as well as by all of our directors and executive officers as a group. The information on beneficial ownership in the table and related footnotes is based upon data furnished to us by, or on behalf of, the persons referred to in the table. Unless otherwise indicated in the footnotes to the table, each person named has sole voting power and sole investment power with respect to the shares included in the table.

| Name   | Beneficial Ownership of Common Stock              |  |                                       | Percent of Class(1) |
|--|---|--|---------------------------------------|---------------------|
|  | Common Stock Beneficially Owned Excluding Options | Stock Options Exercisable within 60 Days of March 18, 2011 | Total Common Stock Beneficially Owned |                     |
| Elliot Noss  | 760,279(2)  | 2,381,804  | 3,142,083                             | 5.6                 |
| Michael Cooperman  | 13,875  | 1,095,975  | 1,109,850                             | 2.0                 |
| David Woroch   | 163,627   | 297,415  | 461,042                               | *                   |
| Stanley Stern  | 203,850   | 147,500  | 351,350                               | *                   |
| Eugene Fiume   |   | 80,000   | 80,000                                | *                   |
| Erez Gissin  | 10,000  | 110,000  | 120,000                               | *                   |
| Joichi Ito   |   | 65,000   | 65,000                                | *                   |
| Allen Karp   | 20,000(3)   | 162,500  | 182,500                               | *                   |
| Lloyd Morrisett  | 105,000(4)  | 182,500  | 287,500                               | *                   |
| Rawleigh Ralls   | 8,450,000(5)                                      | 65,000   | 8,515,000                             | 15.9%               |
| Jeffrey Schwartz   |   | 152,500  | 152,500                               | *                   |
| All directors and executive officers as a group (13 persons) | 9,726,681   | 5,069,194  | 14,795,875                            | 25.3                |

\* Less than 1%.

(1) Based on 53,448,591 shares outstanding as of March 18, 2011, adjusted for shares of common stock beneficially owned but not yet issued.

(2) Includes an aggregate of 245,826 shares of common stock that are indirectly owned by Mr. Noss. Of these shares, Mr. Noss and his wife share investment and voting power over 158,957 shares held in three RRSP accounts belonging to Mr. Noss' wife, 78,957 shares are held in Mr. Noss' RRSP account and 86,869 shares are held by two separate family trusts for which Mr. Noss is the trustee.



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- (3) These shares of common stock are directly owned by Mr. Karp's wife.
- (4) These shares of common stock are owned jointly by Dr. Morrisett and his wife.
- (5) Includes an aggregate of 8,325,000 shares of common stock that are indirectly owned by Mr. Ralls. Of these shares, 175,000 shares are held in Mr. Ralls' IRA account and 8,150,000 are held by Lacuna Hedge Fund LLLP ("Lacuna Hedge") and are indirectly owned by Lacuna, LLC ("Lacuna LLC") and Lacuna Hedge GP LLLP ("Lacuna Hedge GP"). Lacuna LLC is the sole general partner of Lacuna Hedge GP, which is the sole general partner of Lacuna Hedge. Neither Lacuna LLC nor Lacuna Hedge GP directly owns any securities of the Company. Each of Lacuna LLC and Lacuna Hedge GP disclaims beneficial ownership of the shares held by Lacuna Hedge, except to the extent of its pecuniary interest therein. Mr. Ralls is a member of Lacuna LLC. Mr. Ralls disclaims beneficial ownership of the shares held by Lacuna Hedge, except to the extent of his pecuniary interest therein.

**Principal shareholders.**

The following table sets forth information with respect to each shareholder known to us to be the beneficial owner of more than 5% of our outstanding common stock as of March 18, 2011.

| Name and Address of Beneficial Owner                                | Beneficial Ownership of<br>Common Stock      |                        |
|---|--|------------------------|
|   | Number of<br>Shares<br>Beneficially<br>Owned | Percent of<br>Class(1) |
| Lacuna, LLC<br>1100 Spruce Street, Suite 202<br>Boulder, CO 80302   | 8,150,000(2)                                 | 15.2%                  |
| Diker GP, LLC<br>745 Fifth Avenue, Suite 1409<br>New York, NY 10151 | 6,724,135(3)                                 | 12.6%                  |
| Elliot Noss<br>96 Mowat Avenue<br>Toronto, ON M6K 3M1               | 3,142,083(4)                                 | 5.6%                   |

- (1) Based on 53,448,591 shares outstanding as of March 18, 2011.
- (2) As disclosed on Form 4, filed with the SEC on March 10, 2011. These shares are held by Lacuna Hedge Fund LLLP ("Lacuna Hedge") and are indirectly owned by Lacuna, LLC ("Lacuna LLC") and Lacuna Hedge GP LLLP ("Lacuna Hedge GP"). Lacuna LLC serves as the sole general partner of Lacuna Hedge GP, which serves as the sole general partner of Lacuna Hedge. Neither Lacuna LLC nor Lacuna Hedge GP directly owns any securities of the Issuer. Each of Lacuna LLC and Lacuna Hedge GP disclaims beneficial ownership of the securities held by Lacuna Hedge, except to the extent of its pecuniary interest therein. Mr. Ralls is a member of Lacuna LLC. Mr. Ralls disclaims beneficial ownership of the securities held by Lacuna Hedge, except to the extent of his pecuniary interest therein.
- (3) As disclosed on Schedule 13G/A, filed with the SEC on February 14, 2011. The shares are held indirectly by Diker Management, LLC, in its capacity as the Registered Investment Adviser of certain managed accounts and funds. Diker Management, LLC is a Registered Investment Adviser and as such disclaims all beneficial ownership of the

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shares and in any case disclaims beneficial ownership of the shares except to the extent of the reporting person's pecuniary interest therein.

(4)

As disclosed on Form 4 filed with the SEC on March 7, 2011. These shares include an aggregate of 245,826 shares of common stock that are indirectly owned by Mr. Noss. Of these shares, Mr. Noss and his wife share investment and voting power over 80,000 shares held in three RRSP accounts belonging to Mr. Noss' wife, 78,957 shares are held in Mr. Noss' two RRSP accounts and 86,869 shares are held by two separate family trusts for which Mr. Noss is the trustee.

**Equity Compensation Plan Information at Fiscal Year Ended December 31, 2010**

| Plan category   | Number of securities<br>to<br>be issued upon<br>exercise<br>of outstanding<br>options,<br>warrants and rights<br>(#) | Weighted average<br>exercise price of<br>outstanding<br>options,<br>warrants and<br>rights<br>(\$) | Number of securities<br>remaining available for<br>future issuance under<br>the<br>plan (excluding<br>securities<br>reflected in the first<br>column)<br>(#) |
|---|--|--|--|
| Equity compensation plans<br>approved by security holders:    |  |  |  |
| 2006 Equity Compensation Plan                                 | 4,110,000  | \$ 0.69  | 2,778,700  |
| 1996 Equity Compensation Plan                                 | 4,162,249  | \$ 0.42  |  |
| Equity compensation plans not<br>approved by security holders |  |  |  |
| <b>Total</b>  | <b>8,272,249</b>   | <b>\$ 0.56</b>   | <b>2,778,700</b>   |

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE****Review, Approval or Ratification of Transactions with Related Persons**

The Audit Committee of the Board of Directors is responsible for reviewing and, if appropriate, approving all related party transactions between us and any officer or director that would potentially require disclosure pursuant to the Audit Committee charter. As of the date of this Annual Report on Form 10-K, we expect that any transactions in which related persons have a direct or indirect interest will be presented to the Audit Committee for review and approval. While neither the Audit Committee nor the board have adopted a written policy regarding related party transactions, the Audit Committee makes inquiries to our management and our auditors when reviewing such transactions. Neither we nor the audit committee are aware of any transaction that was required to be reported with the SEC where such policies and procedures either did not require review or were not followed.

**Director Independence**

Our Board of Directors has determined that each of Messrs. Stern, Fiume, Gissin, Ito, Karp, Ralls, Schwarz, and Dr. Morrisett are independent directors as defined in Section 121A of the NYSE Amex listing standards. In this Annual Report on Form 10-K, each of these eight directors are referred to individually as an "independent director" and collectively as the "independent directors."

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A summary of the fees of KPMG LLP for the years ended December 31, 2010 and 2009 are set forth below:

|                    | 2010 Fees         | 2009 Fees         |
|--------------------|-------------------|-------------------|
| Audit Fees(1)      | \$ 224,000        | \$ 229,000        |
| Audit-Related Fees | 6,000             |                   |
| Tax Fees(2)        | 91,000            | 95,000            |
| All Other Fees     |                   |                   |
| <b>Total Fees</b>  | <b>\$ 321,000</b> | <b>\$ 324,000</b> |

- 
- (1) Consists of fees and expenses for the audit of consolidated financial statements, the reviews of our quarterly reports on Form 10-Q and services associated with registration statements.
- (2) Consists of fees and expenses for tax consulting services.

**Audit Committee pre-approval of audit and permissible non-audit services of independent auditors.**

The Audit Committee has adopted a pre-approval policy that provides guidelines for the audit, audit-related, tax and other non-audit services that may be provided to us by our independent auditors. Under this policy, the audit committee pre-approves all audit and certain permissible accounting and non-audit services performed by the independent auditors. These permissible services are set forth on an attachment to the policy that is updated at least annually and may include audit services, audit-related services, tax services and other services. For audit services, the independent auditor provides the audit committee with an audit plan including proposed fees in advance of the annual audit. The Audit Committee approves the plan and fees for the audit.

With respect to non-audit and accounting services of our independent auditors that are not pre-approved under the policy, the employee making the request must submit the request to our chief financial officer. The request must include a description of the services, the estimated fee, a statement that the services are not prohibited services under the policy and the reason why the employee is requesting our independent auditors to perform the services. If the aggregate fees for such services are estimated to be less than or equal to \$25,000, our chief financial officer will submit the request to the chairman of the audit committee for consideration and approval, and the engagement may commence upon the approval of the chairman. The chairman is required to inform the full audit committee of the services at its next meeting. If the aggregate fees for such services are estimated to be greater than \$25,000, our chief financial officer will submit the request to the full audit committee for consideration and approval, generally at its next meeting or special meeting called for the purpose of approving such services. The engagement may only commence upon the approval of full audit committee.

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**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

The following documents are filed as part of this Form 10-K:

1. Financial Statements. The financial statements listed in the accompanying index to consolidated financial statements are filed as part of this Form 10-K.

2. Financial Statement Schedules. Schedules are not submitted because they are not required or are not applicable, or the required information is shown in the consolidated financial statements or notes thereto.

3. Exhibits. The Exhibits listed below are filed or incorporated by reference as part of this Form 10-K. Where so indicated by footnote, exhibits which were previously filed are incorporated by reference. For exhibits incorporated by reference, the location of the exhibit in the previous filing is indicated in the footnotes below.

| <b>Exhibit No.</b> | <b>Description</b>  |
|--------------------|---|
| 3.1                | Fourth Amended and Restated Articles of Incorporation of Tucows Inc. (Incorporated by reference to Exhibit 3.1 filed with Tucows' current report on Form 8-K, as filed with the SEC on November 29, 2007).  |
| 3.2                | Second Amended and Restated Bylaws of Tucows Inc. (Incorporated by reference to Exhibit 3.2 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2006, as filed with the SEC on March 29, 2007).   |
| 10.1*              | 2006 Equity Compensation Plan, as amended and restated effective as of July 29, 2010 (Incorporated by reference to Exhibit 99(d)(1) filed with Tucows' Schedule TO, as filed with the SEC on September 17, 2010).   |
| 10.2*              | Employment Agreement dated January 22, 2003 between Tucows.com Co. and Elliot Noss (Incorporated by reference to Exhibit 10.5 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2003, as filed with the SEC on March 28, 2004).                         |
| 10.3*              | Employment Agreement dated March 11, 2003 between Tucows.com Co. and Michael Cooperman (Incorporated by reference to Exhibit 10.5 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2003, as filed with the SEC on March 28, 2004).                     |
| 10.4               | Lease between 707932 Ontario Limited and Tucows International Corporation, dated December 10, 1999 (Incorporated by reference to exhibit number 10.9 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2001, as filed with the SEC on April 1, 2002).   |
| 10.5               | Lease extension between 707932 Ontario Limited and Tucows Inc. and Tucows.com Co., dated September 4, 2004 (Incorporated by reference to Exhibit 10.5 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2004, as filed with the SEC on March 24, 2005). |
| 10.6*              | Description of Tucows Fiscal 2004 At Risk Compensation Plan (Incorporated by reference to Exhibit 10.9 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2004, as filed with the SEC on March 24, 2005).  |
| 10.7#              | Registrar Accreditation Agreement, effective as of June 25, 2005, as amended June 22, 2009, by and between the Internet Corporation for Assigned Names and Numbers and Tucows.com Co.   |

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| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 10.8               | Registry-Registrar Agreement, dated as of October 4, 2001, by and between VeriSign, Inc. and Tucows Inc. (Incorporated by reference to Exhibit 10.13 filed with Amendment No. 1 to Tucows' registration statement on Form S-1 (Registration No. 333-125843), as filed with the SEC on July 7, 2005).                                       |
| 10.11              | Loan Agreement, dated as of June 25, 2007, by and among Tucows.com Co., Tucows (Delaware) Inc., Tucows Inc., Mailbank Nova Scotia Co., Tucows Domain Holdings Co., Innerwise, Inc. and Bank of Montreal (Incorporated by reference to Exhibit 10.1 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007). |
| 10.12              | Guaranty, dated July 25, 2007, by Tucows Inc. in favor of Bank of Montreal (Incorporated by reference to Exhibit 10.2 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007).  |
| 10.13              | Security Agreement, dated July 25, 2007, by Tucows Inc. in favor of Bank of Montreal (Incorporated by reference to Exhibit 10.3 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007).  |
| 10.14              | Financing Commitment, dated July 19, 2007, by and between Tucows.com Co. and Bank of Montreal (Incorporated by reference to Exhibit 10.3 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007).   |
| 10.15              | Operating Loan Agreement, dated September 10, 2010, between Tucows.com Co. and the Bank of Montreal. (Incorporated by reference to Exhibit 10.1 filed with Tucows' current report on Form 8-K, as filed with the SEC on September 13, 2010).   |
| 10.16              | Offer Letter, dated August 30, 2010, between Tucows Inc. and the Bank of Montreal. (Incorporated by reference to Exhibit 10.2 filed with Tucows' current report on Form 8-K, as filed with the SEC on September 13, 2010).   |
| 21.1#              | Subsidiaries of Tucows Inc.  |
| 23.1#              | Consent of KPMG LLP, Independent Registered Public Accounting Firm.  |
| 31.1#              | Chief Executive Officer's Rule 13a-14(a)/15d-14(a) Certification.  |
| 31.2#              | Chief Financial Officer's Rule 13a-14(a)/15d-14(a) Certification.  |
| 32.1#              | Chief Executive Officer's Section 1350 Certification.  |
| 32.2#              | Chief Financial Officer's Section 1350 Certification.  |



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**MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934 as amended. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America and includes those policies and procedures that:

Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;

Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America;

Provide reasonable assurance that our receipts and expenditures are being made only in accordance with authorization of our management and directors; and

Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, such as resource constraints, human error, lack of knowledge or awareness and the possibility of intentional circumvention of these controls, internal control over financial reporting may not prevent or detect misstatements. Furthermore, the design of any control system is based, in part, upon assumptions about the likelihood of future events, for which assumptions may ultimately prove to be incorrect. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Our management assessed the effectiveness of its internal control over financial reporting as of December 31, 2010. In making this assessment, management used the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on its assessment, management has concluded that the Company's internal control over financial reporting was effective as of December 31, 2010.

This Annual Report on Form 10-K does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the SEC that permit the Company to provide only management's report in this Annual Report on Form 10-K.

/s/ ELLIOT NOSS

/s/ MICHAEL COOPERMAN

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Elliot Noss  
*President and Chief Executive Officer*  
*(Principal Executive Officer)*

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Michael Cooperman  
*Chief Financial Officer*  
*(Principal Financial Officer)*

March 22, 2011

March 22, 2011  
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**Report of the Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders of Tucows Inc.:

We have audited the accompanying consolidated balance sheets of Tucows Inc. (and subsidiaries) as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 2010. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Tucows Inc. (and subsidiaries) as of December 31, 2010 and 2009, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2010, in conformity with United States generally accepted accounting principles.

/s/ KPMG LLP

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Chartered Accountants, Licensed Public Accountants  
Toronto, Canada

March 18, 2011

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Table of Contents**Tucows Inc.****Consolidated Balance Sheets****(Dollar amounts in U.S. dollars)**

|   | December 31,<br>2010  | December 31,<br>2009  |
|---|-----------------------|-----------------------|
| <b>Assets</b>   |                       |                       |
| Current assets:   |                       |                       |
| Cash and cash equivalents   | \$ 4,205,729          | \$ 9,632,394          |
| Accounts receivable, net of allowance for doubtful accounts of \$60,000 as of December 31, 2010 and \$110,000 as of December 31, 2009 | 3,021,995             | 2,822,045             |
| Prepaid expenses and deposits   | 2,363,876             | 2,498,922             |
| Derivative instrument asset, current portion (note 4)   | 833,960               | 2,107,825             |
| Prepaid domain name registry and ancillary services fees, current portion   | 37,016,871            | 31,596,236            |
| Income taxes recoverable  | 620,000               | 674,000               |
| <b>Total current assets</b>   | <b>48,062,431</b>     | <b>49,331,422</b>     |
| Derivative instrument asset, long-term portion (note 4)   |                       | 96,845                |
| Prepaid domain name registry and ancillary services fees, long-term portion   | 12,820,479            | 12,126,515            |
| Property and equipment (note 5)   | 1,552,349             | 1,986,768             |
| Deferred financing charges  | 15,600                | 41,000                |
| Deferred tax asset, long-term portion (note 11)   | 4,155,600             | 3,907,476             |
| Intangible assets (note 6)  | 16,883,401            | 18,656,353            |
| Goodwill (note 3)   | 17,990,807            | 17,990,807            |
| <b>Total assets</b>   | <b>\$ 101,480,667</b> | <b>\$ 104,137,186</b> |
| <b>Liabilities and Stockholders' Equity</b>   |                       |                       |
| Current liabilities:  |                       |                       |
| Accounts payable  | \$ 1,664,006          | \$ 1,547,863          |
| Accrued liabilities   | 1,346,436             | 1,889,980             |
| Customer deposits   | 3,960,312             | 3,624,317             |
| Loan payable, current portion (note 7)  | 1,305,883             | 3,220,125             |
| Deferred revenue, current portion   | 45,832,374            | 40,211,766            |
| Accreditation fees payable, current portion   | 547,810               | 530,656               |
| Deferred tax liability, current portion (note 11)   | 1,155,600             | 907,476               |
| <b>Total current liabilities</b>  | <b>55,812,421</b>     | <b>51,932,183</b>     |
| Deferred revenue, long-term portion   | 16,738,429            | 16,098,812            |
| Accreditation fees payable, long-term portion   | 168,580               | 169,620               |
|   | 4,840,000             | 4,840,000             |

Deferred tax liability, long-term  
portion (note 11)

Stockholders' equity (note 9)

Preferred stock no par value,  
1,250,000 shares authorized; none  
issued and outstanding

Common stock no par value,  
250,000,000 shares authorized;  
53,448,591 shares issued and  
outstanding as of December 31,  
2010 and 67,080,353 shares issued  
and outstanding as of December 31,  
2009

|                            |              |              |
|----------------------------|--------------|--------------|
|                            | 11,324,866   | 14,030,384   |
| Additional paid-in capital | 40,700,587   | 47,287,351   |
| Deficit                    | (28,104,216) | (30,221,164) |

|                            |            |            |
|----------------------------|------------|------------|
| Total stockholders' equity | 23,921,237 | 31,096,571 |
|----------------------------|------------|------------|

Total liabilities and stockholders'  
equity

|                |                |
|----------------|----------------|
| \$ 101,480,667 | \$ 104,137,186 |
|----------------|----------------|

Commitments and contingencies  
(note 14)

Subsequent events (note 16)

See accompanying notes to consolidated financial statements

Table of Contents**Tucows Inc.****Consolidated Statements of Operations****(Dollar amounts in U.S. dollars)**

|  | <b>Year ended December 31,</b> |                      |                     |
|--|--------------------------------|----------------------|---------------------|
|  | <b>2010</b>                    | <b>2009</b>          | <b>2008</b>         |
| Net revenues (note 17)   | \$ 84,578,505                  | \$ 80,939,212        | \$ 78,467,880       |
| Cost of revenues (note 17):  |                                |                      |                     |
| Cost of revenues   | 58,494,849                     | 53,187,917           | 47,842,480          |
| Network expenses(*)  | 4,648,899                      | 4,748,189            | 6,771,556           |
| Depreciation of property and equipment                               | 1,032,368                      | 1,673,191            | 2,909,853           |
| Amortization of intangible assets                                    | 299,208                        | 116,796              | 163,796             |
| <b>Total cost of revenues</b>  | <b>64,475,324</b>              | <b>59,726,093</b>    | <b>57,687,685</b>   |
| Gross profit   | 20,103,181                     | 21,213,119           | 20,780,195          |
| Expenses:  |                                |                      |                     |
| Sales and marketing(*)   | 7,217,754                      | 5,812,007            | 6,668,884           |
| Technical operations and development(*)                              | 4,577,898                      | 4,550,704            | 6,172,428           |
| General and administrative(*)  | 2,879,825                      | 5,558,921            | 6,809,601           |
| Depreciation of property and equipment                               | 170,844                        | 266,251              | 263,745             |
| Loss on disposition of property and equipment                        |                                | 40,893               | 498,529             |
| Amortization of intangible assets                                    | 1,442,160                      | 1,442,160            | 1,483,195           |
| Loss (gain) on change in fair value of forward contracts             | 1,370,710                      | (4,179,589)          | 1,974,919           |
| <b>Total expenses</b>  | <b>17,659,191</b>              | <b>13,491,347</b>    | <b>23,871,301</b>   |
| Income (loss) from operations  | 2,443,990                      | 7,721,772            | (3,091,106)         |
| Other income (expense):  |                                |                      |                     |
| Interest expense, net  | (116,197)                      | (225,140)            | (583,911)           |
| Other income, net (note 12)  |                                | 4,493,190            | 5,870,960           |
| <b>Total other income (expense)</b>                                  | <b>(116,197)</b>               | <b>4,268,050</b>     | <b>5,287,049</b>    |
| Income before provision for income taxes                             | 2,327,793                      | 11,989,822           | 2,195,943           |
| Provision for (recovery of) income taxes (note 11)                   | 210,845                        | (251,384)            | 121,134             |
| <b>Net income for the year</b>                                       | <b>\$ 2,116,948</b>            | <b>\$ 12,241,206</b> | <b>\$ 2,074,809</b> |
| Basic earnings per common share (note 2(p))                          | \$ 0.04                        | \$ 0.18              | \$ 0.03             |
| Shares used in computing basic earnings per common share (note 2(p)) | 57,982,248                     | 69,145,001           | 73,817,347          |
| Diluted earnings per common share (note 2(p))                        | \$ 0.04                        | \$ 0.17              | \$ 0.03             |

|  |            |            |            |
|--|------------|------------|------------|
| Shares used in computing diluted earnings per common share (note 2(p)) | 59,955,788 | 70,356,013 | 74,830,217 |
|--|------------|------------|------------|

(\*)

Stock-based compensation has been included in operating expenses as follows:

|                                      |            |            |            |
|--------------------------------------|------------|------------|------------|
| Cost of revenues                     | \$ 22,406  | \$ 15,957  | \$ 19,700  |
| Sales and marketing                  | \$ 96,300  | \$ 58,782  | \$ 64,200  |
| Technical operations and development | \$ 71,012  | \$ 49,302  | \$ 52,700  |
| General and administrative           | \$ 210,284 | \$ 171,220 | \$ 151,200 |

See accompanying notes to consolidated financial statements

Table of Contents**Tucows Inc.****Consolidated Statements of Stockholders' Equity****(Dollar amounts in U.S. dollars)**

|  | <b>Number</b> | <b>Common stock<br/>Amount</b> | <b>Additional<br/>paid in<br/>capital</b> | <b>Deficit</b>  | <b>Total<br/>stockholders'<br/>equity</b> |
|--|---------------|--------------------------------|---|-----------------|---|
| Balances, December 31, 2007                  | 73,888,542    | \$ 15,350,915                  | \$ 48,537,313                             | \$ (44,537,179) | \$ 19,351,049                             |
| Exercise of stock options                    | 35,000        | 17,395                         | (7,945)                                   |                 | 9,450                                     |
| Repurchase and retirement of shares (note 9) | (849,760)     | (169,952)                      | (102,492)                                 |                 | (272,444)                                 |
| Stock-based compensation (note 10)           |               |                                | 287,800                                   |                 | 287,800                                   |
| Net income for the year                      |               |                                |   | 2,074,809       | 2,074,809                                 |
| Balances, December 31, 2008                  | 73,073,782    | 15,198,358                     | 48,714,676                                | (42,462,370)    | 21,450,664                                |
| Exercise of stock options                    | 68,707        | 46,858                         | (21,436)                                  |                 | 25,422                                    |
| Repurchase and retirement of shares (note 9) | (6,074,236)   | (1,214,832)                    | (1,701,150)                               |                 | (2,915,982)                               |
| Issuance of restricted stock                 | 12,600        |                                |   |                 |   |
| Cancellation of restricted stock             | (500)         |                                |   |                 |   |
| Stock-based compensation (note 10)           |               |                                | 295,261                                   |                 | 295,261                                   |
| Net income for the year                      |               |                                |   | 12,241,206      | 12,241,206                                |
| Balances, December 31, 2009                  | 67,080,353    | 14,030,384                     | 47,287,351                                | (30,221,164)    | 31,096,571                                |
| Exercise of stock options                    | 33,678        | 27,350                         | (12,541)                                  |                 | 14,809                                    |
| Repurchase and retirement of shares (note 9) | (13,664,340)  | (2,732,868)                    | (6,974,225)                               |                 | (9,707,093)                               |
| Cancellation of restricted stock             | (1,100)       |                                |   |                 |   |
| Stock-based compensation (note 10)           |               |                                | 400,002                                   |                 | 400,002                                   |
| Net income for the year                      |               |                                |   | 2,116,948       | 2,116,948                                 |
| Balances, December 31, 2010                  | 53,448,591    | \$ 11,324,866                  | \$ 40,700,587                             | \$ (28,104,216) | \$ 23,921,237                             |

See accompanying notes to consolidated financial statements



Table of Contents**Tucows Inc.****Consolidated Statements of Cash Flows****(Dollar amounts in U.S. dollars)**

|   | Year ended December 31, |               |              |
|---|-------------------------|---------------|--------------|
|   | 2010                    | 2009          | 2008         |
| Cash provided by:   |                         |               |              |
| Operating activities:   |                         |               |              |
| Net income for the year                                       | \$ 2,116,948            | \$ 12,241,206 | \$ 2,074,809 |
| Items not involving cash:                                     |                         |               |              |
| Depreciation of property and equipment                        | 1,203,212               | 1,939,442     | 3,173,598    |
| Loss on disposition of property and equipment                 |                         | 40,893        | 498,529      |
| Amortization of deferred financing charges                    | 25,400                  | 37,500        | 49,700       |
| Amortization of intangible assets                             | 1,741,368               | 1,558,956     | 1,646,991    |
| Gain on disposal of investment in Afilias                     |                         | (3,890,395)   | (3,090,404)  |
| Reduction in deferred tax liability                           |                         | (556,000)     |              |
| Gain on sale of customer relationships                        |                         |               | (2,091,995)  |
| Disposal of domain names                                      | 31,584                  | 5,462         | 5,030        |
| Unrealized (gain) loss in the fair value of forward contracts | 1,370,710               | (4,179,589)   | 1,974,919    |
| Stock-based compensation                                      | 400,002                 | 295,261       | 287,800      |
| Change in non-cash operating working capital:                 |                         |               |              |
| Accounts receivable   | (199,950)               | 378,317       | 221,818      |
| Prepaid expenses and deposits                                 | 135,046                 | (224,879)     | 858,086      |
| Prepaid domain name registry and ancillary services fees      | (6,114,599)             | (2,654,170)   | (4,829,254)  |
| Income taxes recoverable                                      | 54,000                  | (674,000)     |              |
| Accounts payable  | (35,210)                | (172,582)     | (789,425)    |
| Accrued liabilities   | (571,930)               | (110,166)     | (1,288,941)  |
| Customer deposits   | 335,995                 | 305,076       | 51,457       |
| Deferred revenue  | 6,260,225               | 2,122,953     | 3,574,397    |
| Accreditation fees payable                                    | 16,114                  | 2,354         | 33,487       |
| Net cash provided by operating activities                     | 6,768,915               | 6,465,639     | 2,360,602    |
| Financing activities:   |                         |               |              |
| Proceeds received on exercise of stock options                | 14,809                  | 25,422        | 9,450        |
| Repurchase of shares  | (9,707,093)             | (2,915,982)   | (272,444)    |
| Repayment of loan payable                                     | (1,914,242)             | (2,639,242)   | (8,914,241)  |
| Net cash (used in) financing activities                       | (11,606,526)            | (5,529,802)   | (9,177,235)  |
| Investing activities:   |                         |               |              |
| Cost of domain names acquired                                 |                         | (13,775)      | (8,944)      |
| Additions to property and equipment                           | (589,054)               | (807,530)     | (2,113,904)  |
| Proceeds on disposition of property and equipment             |                         |               | 66,039       |
| Acquisition of Innerwise Inc., net of cash acquired           |                         |               | (500,000)    |
| Proceeds on disposal of shares in Afilias Inc.                |                         | 4,090,395     | 3,244,141    |
| Sale of customer relationships                                |                         |               | 2,392,660    |
| Decrease (increase) in cash held in escrow                    |                         |               | 1,070,632    |
| Net cash (used in) provided by investing activities           | (589,054)               | 3,269,090     | 4,150,624    |
| (Decrease) increase in cash and cash equivalents              | (5,426,665)             | 4,204,927     | (2,666,009)  |
| Cash and cash equivalents, beginning of year                  | 9,632,394               | 5,427,467     | 8,093,476    |

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Cash and cash equivalents, end of year \$ 4,205,729 \$ 9,632,394 \$ 5,427,467

Supplemental cash flow information:

Interest paid \$ 116,242 \$ 227,616 \$ 630,729

Income taxes paid \$ 200,685 \$ 1,165,000 \$ 182,876

Supplementary disclosure of non-cash investing and financing activities:

Property and equipment acquired during the period not yet paid for \$ 273,333 \$ 93,594 \$ 6,979

See accompanying notes to consolidated financial statements

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**Tucows Inc.**

**Notes to Consolidated Financial Statements**

**(Dollar Amounts in U.S. dollars)**

**1. Organization of the Company:**

Tucows Inc. (the "Company") is a global distributor of Internet services, including domain name registration, security and identity products through digital certificates and email through its global Internet-based distribution network of Internet Service Providers, web hosting companies and other providers of Internet services to end-users.

**2. Significant accounting policies:**

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and are stated in U.S. dollars, except where otherwise noted. Certain of the prior year comparative figures have been reclassified to conform with the financial statement presentation adopted in the current year.

*(a) Basis of presentation*

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated on consolidation.

Investments over which the Company is unable to exercise significant influence, are recorded at cost and written down only when there is evidence that a decline in value that is other than temporary has occurred.

During fiscal 2010, the Company corrected two immaterial errors relating to prior annual periods. Amortization of intangible assets of \$0.2 million relating to acquired technology was cumulatively understated during prior annual periods, and rent expense was cumulatively understated by \$0.1 million as at the end of fiscal 2009. As a result of these corrections, the amortization of intangible assets and general and administrative expense for the year ended December 31, 2010 are over stated, by \$0.2M and \$0.1M respectively and retained earnings is properly stated.

*(b) Use of estimates*

The preparation of the consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, management evaluates its estimates, including those related to amounts recognized for or carrying values of revenues, bad debts, investments, goodwill and intangible assets which require estimates of future cash flows and discount rates, income taxes, contingencies and litigation, and estimates of credit spreads for determination of the fair value of derivative instruments. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances at the time they are made. Under different assumptions or conditions, the actual results will differ, potentially materially, from those previously estimated. Many of the conditions impacting these assumptions and estimates are outside of the Company's control.

*(c) Cash and cash equivalents*

All highly liquid investments, with an original term to maturity of three months or less are classified as cash and cash equivalents.

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****2. Significant accounting policies: (Continued)***(d) Property and equipment*

Property and equipment are stated at cost, net of accumulated amortization. Amortization is provided on a straight-line basis so as to amortize the cost of depreciable assets over their estimated useful lives at the following rates:

| <b>Asset</b>            | <b>Rate</b>        |
|-------------------------|--------------------|
| Computer equipment      | 30%                |
| Computer software       | 100%               |
| Furniture and equipment | 20%                |
| Leasehold improvements  | Over term of lease |

The Company reviews the carrying values of its property and equipment for potential impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the estimated undiscounted future cash flows expected to result from the use of the group of assets and its eventual disposition is less than its carrying amount, it is considered to be impaired. The amount of the impairment loss recognized is measured as the amount by which the carrying value of the asset exceeds the fair value of the asset, with fair value being determined based upon discounted cash flows or appraised values, depending on the nature of the assets.

*(e) Goodwill and Intangible assets*

Goodwill represents the excess of purchase price over the fair values assigned to the net assets acquired in business combinations. Intangible assets consist of acquired technology, brand, customer relationships, non-competition agreements, surname domain names and direct navigation domain names. Intangible assets, comprising technology, brand value, customer relationships and non-competition arrangements related to the acquisition of Boardtown Corporation in April 2004, the acquisition of the Hosted Messaging Business of Critical Path, Inc. in January 2006, the acquisition of Mailbank.com Inc. in June 2006 and the acquisition of Innerwise, Inc. in June 2007, are being amortized on a straight-line basis over periods of two to seven years.

The Company does not amortize goodwill and indefinite life intangibles, but tests for impairment annually or more frequently if circumstances indicate potential impairment, through a comparison of fair value to its carrying amount. The Company reviews goodwill at least annually for possible impairment in the fourth quarter of each year.

Goodwill is tested for impairment as part of a two-step process. The first step uses a market approach that is based on the publicly traded common shares of the Company to estimate fair value. If the carrying value is less than the fair value, no impairment exists and the second step need not be performed. If the carrying value is greater than the fair value then the second step will be performed. In the second step, the impairment is computed by comparing the implied fair value of the Company's goodwill with the carrying amount of that goodwill.

For the second step the Company uses a discounted cash flow or income approach in which future expected cash flows are converted to present value using factors that consider the timing and risk of the future cash flows. The estimate of cash flows used is prepared on an unleveraged debt-free basis. The discount rate reflects a market-derived weighted average cost of capital. The Company believes

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**2. Significant accounting policies: (Continued)**

that this approach is appropriate because it provides a fair value estimate based upon the Company's expected long-term operating and cash flow performance. The projections are based upon the Company's best estimates of projected economic and market conditions over the related period including growth rates, estimates of future expected changes in operating margins and cash expenditures.

Other significant estimates and assumptions include terminal value growth rates, terminal value margin rates, future capital expenditures and changes in future working capital. If assumptions and estimates used to allocate the purchase price or used to assess impairment prove to be inaccurate, future asset impairment charges could be required. At December 31, 2010, the Company had goodwill of \$18.0 million. The Company completed its latest annual impairment test and fair value analysis for goodwill, and there were no impairments present and no impairment charge was recorded during the years ended December 31, 2010, 2009 and 2008.

The Company has other finite life intangible assets consisting of patented and non-patented technologies. These intangible assets are amortized over their expected economic lives. The lives are determined based upon the expected use of the asset, the estimated average life of the replacement parts of the reporting units products, the stability of the industry, expected changes in and replacement value of distribution networks and other factors deemed appropriate.

The Company continually evaluates whether events or circumstances have occurred that indicate the remaining estimated useful lives of its definite-lived intangible assets may warrant revision or that the remaining balance of such assets may not be recoverable. The Company uses an estimate of the related undiscounted cash flows over the remaining life of the asset in measuring whether the asset is recoverable. There was no impairment recorded on definite-life intangible assets and other long-lived assets during 2010 and 2009.

*(f) Revenue recognition*

The Company's revenues are derived from domain name registration fees on both a wholesale and retail basis, the sale of domain names, the provisioning of other Internet services and advertising and other revenue. Amounts received in advance of meeting the revenue recognition criteria described below are recorded as deferred revenue.

The Company earns registration fees in connection with each new, renewed and transferred-in registration and from providing provisioning of other Internet services to resellers and registrars on a monthly basis. Service has been provided in connection with registration fees once the Company has confirmed that the requested domain name has been appropriately recorded in the registry under contractual performance standards.

Domain names are generally purchased for terms of one to ten years. Registration fees charged for domain name registration and provisioning services are recognized on a straight-line basis over the life of the contracted term. Registration fee revenues are net of any promotional rebates as the Company has a continuing obligation to provide services to customers throughout the registration period. Other Internet services that are provisioned for annual periods or longer, are recognized on a straight-line bases over the life of the contracted term. Other Internet services that are provisioned on a monthly basis are recognized as services are provided.

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**2. Significant accounting policies: (Continued)**

Revenue generated from the sale of domain names, earned from transferring the rights to domain names under the Company's control, are recognized once payment has been received in full.

The Company also generates advertising and other revenue through its online libraries of shareware, freeware and online services presented on its website. Advertising and other revenues are recognized ratably over the period in which it is presented. To the extent that minimum guaranteed impressions are not met, the Company defers recognition of the corresponding revenues until the guaranteed impressions are achieved.

In those cases where payment is not received at the time of sale, additional conditions for recognition of revenue are that the collection of the related accounts receivable is reasonably assured and the Company has no further performance obligations. The Company records costs that reflect expected refunds, rebates and credit card charge-backs as a reduction of revenues at the time of the sale based on historical experiences and current expectations.

The Company establishes reserves for possible uncollectible accounts receivable and other contingent liabilities which may arise in the normal course of business. Historically, credit losses have been within the Company's expectations and the reserves the Company has established have been appropriate. However, the Company has, on occasion, experienced issues which have led to accounts receivable not being fully collected. Should these issues occur more frequently, additional reserves may be required.

*(g) Deferred revenue*

Deferred revenue primarily relates to the unearned portion of revenues received in advance related to the unexpired term of registration fees from domain name registrations and other Internet services, on both a wholesale and retail basis, net of external commissions. Revenue received in advance of the provision of services from our software libraries advertising is deferred and recognized in the month that the services are provided.

*(h) Accreditation fees payable*

In accordance with ICANN rules, the Company has elected to pay ICANN fees incurred on the registration of Generic Top-Level Domains on an annual basis. Accordingly, accreditation fees that relate to registrations completed prior to ICANN rendering a bill are accrued and reflected as accreditation fees payable.

*(i) Prepaid domain name registry fees*

Prepaid domain name registry and other Internet services fees represent amounts paid to registries, and country code domain name operators for updating and maintaining the registries, as well as to suppliers of other Internet services. Domain name registry and other Internet services fees are recognized on a straight-line basis over the life of the contracted registration term.

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**2. Significant accounting policies: (Continued)**

*(j) Translation of foreign currency transactions*

The Company's functional currency is the United States dollar. Monetary assets and liabilities of the Company and of its wholly owned subsidiaries that are denominated in foreign currencies are translated into United States dollars at the exchange rates prevailing at the balance sheet dates. Non-monetary assets and liabilities are translated at the historical exchange rates. Transactions included in operations are translated at the average rate for the year. A foreign exchange gain amounting to \$2.3 million has been recorded in general and administrative expenses in the consolidated statements of operations during the year ended December 31, 2010. A foreign exchange loss amounting to \$0.7 million has been recorded in general and administrative expenses in the consolidated statements of operations during the year ended December 31, 2009. A foreign exchange loss amounting to \$0.8 million has been recorded in general and administrative expenses in the consolidated statements of operations during the years ended December 31, 2008.

*(k) Derivative Instruments*

The Company has not complied with the documentation standards required for its forward foreign exchange contracts to be accounted for as hedges and has, therefore, accounted for such forward foreign exchange contracts at their fair values with the changes in fair value recorded in the consolidated statements of operations. The fair value of the forward exchange contracts are determined using an estimated credit-adjusted mark-to-market valuation which takes into consideration the Company and the counterparty credit risk.

*(l) Fair Value Measurements of Assets and Liabilities*

The Company accounts for all financial assets and financial liabilities and for all non-financial assets and non-financial liabilities recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Carrying amounts of certain financial instruments, including cash and cash equivalents, accounts receivable and accounts payable (trade and accrued liabilities) approximate their fair value due to the relatively short period of time between origination of the instruments and their expected realization. See Note 15 for further details on fair value measurements.

*(m) Product development costs*

Product development costs are expensed as incurred. The Company accounts for the costs of computer software developed or obtained for internal use as follows: costs that are incurred in the preliminary stage of software development are expensed as incurred. Costs incurred during the application and development stage are capitalized and generally include external direct costs of materials and services consumed in the development and payroll and payroll-related costs for employees who are directly associated with the development project. Costs incurred in the post implementation and operation stage are expensed as incurred. During the years ended December 31, 2010, 2009 and 2008, the Company did not capitalize any amounts of such costs relating to the development of internal use software. The capitalized costs of computer software developed for internal use are amortized on a straight-line basis over one year from the date the software is put into use.

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**2. Significant accounting policies: (Continued)**

*(n) Income taxes*

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the consolidated statement of operations in the year that includes the enactment date. A valuation allowance is recorded if it is not "more likely than not" that some portion of or all of a deferred tax asset will be realized.

The Company recognizes the impact of an uncertain income tax position at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority and includes consideration of interest and penalties. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. The liability for unrecognized tax benefits is classified as non-current unless the liability is expected to be settled in cash within 12 months of the reporting date.

The Company is entitled to earn investment tax credits ("ITCs"), which are credits related to specific qualifying expenditures as prescribed by Canadian Income Tax legislation. These ITCs relate primarily to research and development expenses. The ITCs are recognized as a reduction in income tax expense once the Company has reasonable assurance that the amounts will be realized.

*(o) Stock-based compensation*

Stock-based compensation expense recognized during the period is based on the value of the portion of stock-based payment awards that is ultimately expected to vest. As stock-based compensation expense recognized in the statement of operations for 2010 is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures.

*(p) Earnings per common shares*

Basic earnings per common share has been calculated on the basis of income for the year divided by the weighted average number of common shares outstanding during each year. Diluted earnings per share gives effect to all dilutive potential common shares outstanding at the end of the year had been issued, converted or exercised at the later of the beginning of the year or their date of issuance. In computing diluted earnings per share, the treasury stock method is used to determine the number of shares assumed to be purchased from the conversion of common shares equivalents or the proceeds of exercises of options.

*(q) Concentration of credit risk*

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash equivalents, restricted cash, accounts receivable and forward foreign exchange contracts. Cash equivalents and restricted cash consist of deposits with major commercial banks, the maturities of which are three months or less from the date of purchase. With respect to accounts receivable, the Company performs periodic credit evaluations of the financial condition of its customers and typically does not require collateral from them. The counterparty to any forward foreign exchange



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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**2. Significant accounting policies: (Continued)**

contracts is a major commercial bank which management believes does not represent a significant credit risk. Management assesses the need for allowances for potential credit losses by considering the credit risk of specific customers, historical trends and other information. No customer accounted for more than 10% of revenue in 2010, 2009 or 2008. Three customers accounted for 35% of accounts receivable at December 31, 21010, one customer accounted for 11% of accounts receivable at December 31, 2009, and two customers accounted for 20% of accounts receivable at December 31, 2008. All of these accounts receivable have subsequently been collected.

*(r) Fair values of financial assets and financial liabilities*

The carrying values of cash and cash equivalents, restricted cash, accounts receivable, accounts payable, accreditation fees payable, customer deposits and accrued liabilities approximate their fair values due to the relatively short periods to maturity of the instruments.

The fair value of the forward exchange contracts are determined using an estimated credit-adjusted mark-to-market valuation which takes into consideration the Company and the counterparty credit risk.

*(s) Comprehensive income*

Items of their comprehensive income are classified by their nature in the financial statements and display the accumulated balance of other comprehensive income separately from deficit and additional paid-in capital in the equity section of the balance sheet. There was no difference between net income and comprehensive income for the years ended December 31, 2010, 2009 and 2008.

*(t) Segment reporting*

The Company operates in one business segment.

The Company's revenues are attributed to the country in which the contract originates, primarily Canada. Revenues from domain names issued from the Toronto, Canada location are attributed to Canada because it is impracticable to determine the country of the customer.

The Company's assets are located in Canada, United States of America and United Kingdom (see note 17).

*(u) Recent accounting pronouncements*

No new accounting pronouncements have been adopted during Fiscal 2010. *Recent Accounting Pronouncements Not Yet Adopted*

In October 2009, the FASB issued Accounting Standards Update 2009-13, "Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements" ("Update 2009-13"). Update 2009-13 applies to multiple-deliverable revenue arrangements that are currently within the scope of FASB ASC Subtopic 605-25 (previously included in Emerging Issues Task Force Issue no. 00-21, "Revenue Arrangements with Multiple Deliverables"). Update 2009-13 provides principles and application guidance on whether multiple deliverables exist, how the arrangement should be separated, and the consideration allocated. It also requires an entity to allocate revenue in an arrangement using estimated selling prices of deliverables if a vendor does not have vendor-specific objective evidence or third-party

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**2. Significant accounting policies: (Continued)**

evidence of selling price. The guidance eliminates the use of the residual method, requires entities to allocate revenue using the relative-selling-price method, and significantly expands the disclosure requirements for multiple-deliverable revenue arrangements. Update 2009-13 is effective on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. We are currently assessing the impact of Update 2009-13 on our future consolidated financial statements.

**3. Business acquisitions:**

**a.**

**Acquisition of Innerwise, Inc. (dba *ItsYourDomain.com*):**

On July 25, 2007, Tucows (Delaware) Inc. ("Tucows DE"), one of the Company's wholly owned subsidiaries, acquired 100% of the outstanding capital stock of Innerwise, Inc. (d/b/a *ItsYourDomain.com*) ("IYD"), a privately held, ICANN-accredited registrar offering domain services through a worldwide wholesale network of over 2,500 affiliates. The total aggregate consideration amounting to \$11,450,112 is comprised of:

\$10,847,650 paid in cash;

\$102,462 of estimated transaction costs, and

\$500,000 released from escrow in 2008.

An additional \$1.1 million of consideration was held in escrow, and was payable in whole or in part by Tucows in August 2008, pending the final evaluation of the revenue generating capability of certain domain names acquired by Tucows DE under the purchase agreement, as well as the resolution of any indemnification claims made by Tucows DE, for which the escrow account also served as a source of recovery.

During Fiscal 2008, the escrow account of \$1.1 million was resolved and distributed. \$500,000 of the monies in escrow were released to the former shareholders of Innerwise, Inc. as the final evaluation of the revenue generating capability of certain domain names originally acquired by Tucows DE under the purchase agreement, as well as the resolution of any indemnification claims made by Tucows DE, for which the escrow account served as a source of recovery was resolved. This additional contingent consideration was recorded as additional goodwill in Fiscal 2008. \$500,000 of the remaining escrow was released and distributed to Tucows, and the remaining balance of \$0.1 million was donated to various charities.

\$9,571,209 of the cash paid by Tucows at the closing was funded by a bank loan from a Canadian chartered bank (see note 7).

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****3. Business acquisitions: (Continued)**

The allocation of the fair value of the net assets acquired based on the consideration paid, is as follows:

|                               |    |           |            |
|-------------------------------|----|-----------|------------|
| Cash and cash equivalents     | \$ | 618,047   |            |
| Accounts receivable           |    | 26,224    |            |
| Prepaid expenses and deposits |    | 252,128   |            |
| Property and equipment        |    | 20,000    |            |
| Intangible assets including:  |    |           |            |
| Technology                    | \$ | 350,000   |            |
| Brand                         |    | 1,000,000 |            |
| Customer relationships        |    | 3,700,000 | 5,050,000  |
| Goodwill                      |    |           | 5,801,040  |
| Total assets acquired         |    |           | 11,767,439 |
| Accrued liabilities           |    | 317,327   |            |
| Total liabilities             |    |           | 317,327    |
| Purchase price                | \$ |           | 11,450,112 |

The residual value from the purchase price has been allocated to goodwill. The technology is being amortized over 3 years, while the remaining intangible assets are being amortized over 7 years.

The valuation of the intangible assets is management's best estimate, based, in part, on a report from an independent valuator. Any changes to the value assigned to the acquired assets, as a result of any adjustments to working capital, will be reflected by an equal and offsetting adjustment to goodwill.

**b.****Goodwill:**

Goodwill represents the excess of purchase price over the fair value of tangible or identifiable intangible assets acquired and liabilities assumed in our acquisitions. Intangible assets consist of acquired technology, brand, customer relationships, non-competition agreements, surname domain names and direct navigation domain names. Intangible assets, comprising technology, brand value, customer relationships and non-competition arrangements related to the acquisition of Boardtown Corporation in April 2004, the acquisition of the Hosted Messaging Business of Critical Path, Inc. in January 2006, the acquisition of Mailbank.com Inc. in June 2006 and the acquisition of Innerwise, Inc. in July 2007, are being amortized on a straight-line basis over periods of two to seven years.

The Company has other finite life intangible assets consisting of patented and non-patented technologies. These intangible assets are amortized over their expected economic lives. The lives are determined based upon the expected use of the asset, the estimated average life of the replacement parts of the reporting units products, the stability of the industry, expected changes in and replacement value of distribution networks and other factors deemed appropriate.

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****3. Business acquisitions: (Continued)**

Goodwill consists of the following:

|   | <b>Boardtown<br/>Corporation</b> | <b>Hosted<br/>Messaging<br/>Assets of<br/>Critical Path</b> | <b>Innerwise<br/>Inc.</b> | <b>Mailbank.com<br/>Inc.</b> | <b>Total</b>  |
|---|----------------------------------|---|---------------------------|------------------------------|---------------|
| Balances, December 31, 2008             | 2,044,847                        | 4,072,297   | 5,801,040                 | 6,072,623                    | 17,990,807    |
| Balances, December 31, 2009<br>and 2010 | \$ 2,044,847                     | \$ 4,072,297  | \$ 5,801,040              | \$ 6,072,623                 | \$ 17,990,807 |

Goodwill and indefinite life intangibles are not amortized, but are tested for impairment annually or more frequently if circumstances indicate potential impairment, through a comparison of fair value to carrying amount. Goodwill is tested for impairment annually at the same time every year, and when an event occurs or circumstances change such that it is reasonably possible that impairment may exist. The Company reviews goodwill at least annually for possible impairment in the fourth quarter of each year.

With regards to property, equipment and definite life intangible assets, the Company continually evaluates whether events or circumstances have occurred that indicate the remaining estimated useful lives of its definite-life intangible assets may warrant revision or that the remaining balance of such assets may not be recoverable. The Company measures recoverability of assets to be held and used by comparing the carrying amount of the assets to future undiscounted net cash flows expected to be generated by the assets. Recoverability measurement and estimation of undiscounted cash flows is done at the lowest possible levels for which there are identifiable cash flows. If such assets fail the recoverability test, the impairment to be recognized is measured as the amount by which the carrying amount of assets exceeds the fair value of the assets. Assets to be disposed of are recorded at the lower of the carrying amount or fair value less costs to sell. Management must exercise judgment in determining whether an event has occurred that may impair the value of the long-lived assets. Factors that could indicate that impairment may exist include significant underperformance relative to a plan or long-term projections, significant changes in business strategy, significant negative industry or economic trends or a significant decline in our stock price or in the value of our reporting units for a sustained period of time. There was no impairment recorded on definite-life intangible assets and property and equipment during 2010 and 2009.

The Company's 2010 annual goodwill impairment analysis, which the Company performed for its reporting unit as of December 31, 2010, did not result in an impairment charge. The Company determined the estimated fair value of its reporting unit using the income approach and the market approach to determine that the estimated fair value exceeded its carrying value. This analysis was consistent with the approach the Company utilized in its analysis performed in prior years. Determining the number of reporting units and the fair value of a reporting unit requires the Company to make judgments and involves the use of significant estimates and assumptions. These estimates and assumptions include revenue growth rates and operating margins used to calculate projected future cash flows, risk-adjusted discount rates, future economic and market conditions. The key assumptions used in our 2010 annual goodwill impairment test to determine the fair value of the Company's reporting unit included: (a) cash flow projections, which include growth and allocation assumptions for

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****3. Business acquisitions: (Continued)**

forecasted revenue and expenses; (b) a residual growth rate of 3.0%; and (c) a discount rate of 18%, which was based upon the Company's reporting unit's weighted-average cost of capital adjusted for the risks associated with the operations at the time of the assessment. As of the date of our 2010 annual impairment test, the Company's estimated fair values for its reporting unit, based on reasonable changes in assumptions exceed its carrying value by a range of 40% to 80%. The Company believes that the assumptions and estimates used to determine the estimated fair value of its reporting unit are reasonable; however, these estimates are inherently subjective, and there are a number of factors, including factors outside of the Company's control that could cause actual results to materially differ from its estimates. Changes in estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge.

Any changes to the Company's key assumptions about its businesses, prospects, or changes in market conditions, could cause the fair value of its reporting unit to fall below its carrying value, resulting in a potential impairment charge. In addition, changes in its organizational structure or how its management allocates resources and assesses performance, could result in a change in its operating segments or reporting units, requiring a reallocation and updated impairment analysis of goodwill. A goodwill or intangible asset impairment charge could have a material effect on its consolidated financial statements because of the significance of goodwill and intangible assets to its consolidated balance sheet. As of December 31, 2010, the Company had \$18.0 million and \$16.9 million, respectively, in goodwill and intangible assets.

**4. Derivative instrument assets/liabilities:**

The Company enters into foreign currency contracts to hedge a portion of the Company's expected Canadian dollar requirements. All derivative financial instruments are recorded at fair value on our consolidated balance sheet. The fair value of our foreign currency contracts at December 31, 2010 was a net unrealized gain of \$0.8 million (as compared to a net unrealized gain of \$2.2 million at December 31, 2009). The unrealized gains are a result of fluctuations in foreign exchange rates between the date the currency forward contracts were entered into and the valuation date at period end. The net unrealized gain of our foreign currency contracts during the year ended December 31, 2010 is due primarily to the favorable movement in exchange rates between the Canadian and U.S. dollars and the settlement of contracts with significant gains.

At December 31, 2010, the Company had forward exchange contracts to trade U.S. dollars in exchange for Canadian dollars as follows:

| <b>Maturity date</b>    | <b>Notional<br/>amount of<br/>U.S. dollars</b> | <b>Weighted average<br/>exchange rate of<br/>U.S. dollars</b> | <b>Fair value<br/>gain</b> |
|-------------------------|--|---|----------------------------|
| January - March 2011    | \$ 5,400,000                                   | 0.9307  | \$ 430,307                 |
| April - June 2011       | 3,900,000                                      | 0.9635  | 157,943                    |
| July - September 2011   | 3,900,000                                      | 0.9604  | 160,006                    |
| October - November 2011 | 2,700,000                                      | 0.9666  | 85,704                     |
| <b>Total</b>            | <b>\$ 15,900,000</b>                           | <b>0.9399</b>   | <b>\$ 833,960</b>          |

As of December 31, 2009, we had outstanding foreign currency forward contracts amounting to \$25.2 million.

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****4. Derivative instrument assets/liabilities: (Continued)**

As we do not comply with the documentation requirements for hedge accounting, we account for the fair value of the derivative instruments within the consolidated balance sheet as a derivative financial asset or liability and the corresponding change in fair value is recorded in the consolidated statement of operations. We have no other freestanding or embedded derivative instruments.

The Company is not required to apply hedge accounting and, therefore, for the year ended December 31, 2010, the Company recorded a loss of \$1.4 million in the fair value of forward contracts in its consolidated statements of operations. For the year ended December 31, 2009, the Company recorded a gain on forward contracts of \$4.2 million. For the year ended December 31, 2008, the Company recorded a loss of \$2.0 million in the fair value of forward contracts in its consolidated statements of operations.

**5. Property and equipment:**

Property and equipment consist of the following:

|                          | December 31,<br>2010 | December 31,<br>2009 |
|--------------------------|----------------------|----------------------|
| Computer equipment       | \$ 8,262,776         | \$ 8,263,842         |
| Computer software        | 2,600,681            | 2,575,454            |
| Furniture and equipment  | 1,065,980            | 963,031              |
| Leasehold improvements   | 769,606              | 756,287              |
|                          | 12,699,043           | 12,558,614           |
| Less:                    |                      |                      |
| Accumulated amortization | 11,146,694           | 10,571,846           |
|                          | \$ 1,552,349         | \$ 1,986,768         |

Depreciation of property and equipment:

|  | Year ended<br>December 31,<br>2010 | Year ended<br>December 31,<br>2009 | Year ended<br>December 31,<br>2008 |
|--|------------------------------------|------------------------------------|------------------------------------|
| Depreciation of Property and equipment | \$ 1,203,212                       | \$ 1,939,442                       | \$ 3,173,598                       |

**6. Intangible assets:**

Intangible assets consist of acquired technology, brand, customer relationships, non-competition agreements, surname domain names and direct navigation domain names. These balances are being amortized on a straight-line basis over the term of the intangible assets, as reflected in the table below.

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****6. Intangible assets: (Continued)**

Acquired intangible assets consist of the following:

| Amortization period                                 | Technology<br>2 - 7 years | Brand<br>7 years | Customer relationships<br>4 - 7 years | Non-compete agreements<br>3 years | Surname domain names<br>indefinite life | Direct navigation domain names<br>indefinite life | Total         |
|---|---------------------------|------------------|---------------------------------------|-----------------------------------|---|---|---------------|
| Balances, December 31, 2008                         | \$ 441,724                | \$ 853,860       | \$ 4,683,500                          | \$                                | \$ 12,143,595                           | \$ 2,084,317                                      | \$ 20,206,996 |
| Additions to/(disposals from) domain portfolio, net |                           |                  |                                       |                                   | (11,187)                                | 19,500  | 8,313         |
| Amortization expense                                | (116,796)                 | (167,040)        | (1,275,120)                           |                                   |   |   | (1,558,956)   |
| Balances, December 31, 2008                         | 324,928                   | 686,820          | 3,408,380                             |                                   | 12,132,408                              | 2,103,817   | 18,656,353    |
| Additions to/(disposals from) domain portfolio, net |                           |                  |                                       |                                   | (6,490)                                 | (25,094)  | (31,584)      |
| Amortization expense                                | (299,208)                 | (167,040)        | (1,275,120)                           |                                   |   |   | (1,741,368)   |
| Balances, December 31, 2009                         | \$ 25,720                 | \$ 519,780       | \$ 2,133,260                          | \$                                | \$ 12,125,918                           | \$ 2,078,723                                      | \$ 16,883,401 |

The following table shows the estimated amortization expense for each of the next 5 years, assuming no further additions to acquired intangible assets are made:

|       | Year ending<br>December 31, |
|-------|-----------------------------|
| 2011  | \$ 945,860                  |
| 2012  | 670,800                     |
| 2013  | 670,800                     |
| 2014  | 391,300                     |
| Total | \$ 2,678,760                |

Indefinite life intangible assets represent domain names acquired from third parties and surname and direct navigation domain names related to the acquisition of Mailbank.com Inc. in June 2006. These assets are not being amortized and are being tested for impairment annually and whenever events or changes in circumstances indicate that their carrying value may not be recoverable. The Company uses a discounted cash flow or income approach to estimate the fair value of its indefinite life intangible assets. In the discounted cash flow approach, expected cash flows are converted to present value using factors that consider the timing and risk of the future cash flows. The estimate of cash flows used is prepared on an unleveraged debt-free basis. The discount rate reflects a market-derived weighted average cost of capital. The Company believes that this approach is appropriate because it provides a fair value estimate based upon the Company's expected long-term operating and cash flow performance. The projections are based upon the Company's best estimates of projected economic and market conditions over the related period including growth rates, estimates of future expected changes in operating margins and cash expenditures. Other significant estimates and assumptions include terminal value growth rates, terminal value margin rates, future capital

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**6. Intangible assets: (Continued)**

expenditures and changes in future working capital. If assumptions and estimates used to allocate the purchase price or used to assess impairment prove to be inaccurate, future asset impairment charges could be required. At December 31, 2010, the Company had indefinite life assets of \$14.2 million. The Company completed its latest annual impairment test and fair value analysis for indefinite life intangible assets, and there were no impairments present and no impairment charge was recorded during the years ended December 31, 2010, 2009 and 2008.

As part of the Company's decision to divest of non-strategic assets, in June and September 2008, the Company entered into definitive agreements with two purchasers to acquire the Company's retail web hosting end-user websites and customers. The sale of customer relationships with a net book value of \$300,665 resulted in a gain on the sale of these customer relationships of \$2.1 million.

**7. Loan payable:**

The Company has credit agreements with the Bank of Montreal that provides it access to the following facilities:

1. a non-revolving, reducing demand loan facility that was used to fund the acquisition of Innerwise, Inc. during 2007 under which \$1.3 million was owing as of December 31, 2010. This facility is repayable in equal monthly installments of \$159,520 plus interest. The Company can elect to pay interest either at the Bank of Montreal ("BMO") U.S. Base Rate plus 1.30% or at LIBOR plus 3.25%. The Company has elected to pay interest based on LIBOR plus 3.25%. All interest is payable monthly in arrears as incurred. The Company will continue to make annual cash sweep payments to the Bank based on the Company's audited financial statements. Based on the anticipated annual cash sweep payment for Fiscal 2010, the Company expects that the remaining balance will be fully repaid by June 2011;
2. a non-revolving, reducing demand loan facility for \$2.0 million which can be used to finance the repurchase of the Company's common shares. As of December 31, 2010, the Company had no borrowings under this credit facility. Any advances under this facility are repayable in equal monthly installments over 60 months plus interest. This facility is subject, following the first draw, to an undrawn aggregate standby fee of 0.20% which is payable quarterly in arrears. The Company can elect to pay interest either at the Bank of Montreal ("BMO") U.S. Base Rate plus 1.30% or at LIBOR plus 3.25%. All interest is payable monthly in arrears as incurred. This facility will require the Company to make annual cash sweep payments to the Bank based on the Company's audited financial statements;
3. an operating demand loan for \$1.0 million to fund operational requirements. As of December 31, 2010, the Company had no borrowings under this credit facility. The Company has agreed to pay any outstanding principal amounts advanced under this facility, plus interest at a rate of BMO U.S. Base Rate plus 1.30%. Interest is payable monthly in arrears with any borrowing under the facility fluctuating widely with periodic clean-up, at a minimum on an annual basis. The Company has also agreed to pay to the Bank a monthly monitoring fee of \$500. The Operating Demand Loan Facility is payable on demand at any time, at the sole discretion of the Bank, with or without cause; and



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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**7. Loan payable: (Continued)**

4.

a Treasury Risk Management Facility for \$3.5 million to be used as a line to fund any settlement risk exposure that may arise from foreign exchange contracts the Company enters into from time to time to mitigate the exchange rate risk on portions of its Canadian dollar exposure. At December 31, 2010, the Company had forward exchange contracts to trade \$15.9 million U.S. dollars in exchange for Canadian dollars.

Pursuant to the credit agreements, the Company has agreed to comply with certain customary non-financial covenants regarding maintenance of insurance; payment of taxes; disposition of major assets; compliance with statutes and with environmental standards; reporting requirements; timely provision of notices of default; absence of material judgments; access to books and records; prohibition on assumption of additional debt or guarantee obligations by the Company, subject to certain exceptions for capital expenditures; and prohibition on the payment of dividends.

The non-revolving reducing demand loan facilities also require that the Company complies with the following financial covenants: (i) Maximum Senior Funded Debt to EBITDA of 2.00:1; (ii) Maximum Total Funded Debt to EBITDA of 2.50:1; and (iii) Minimum Fixed Charge Coverage of 1.25:1. Further, the Company's Maximum Annual Capital Expenditures cannot exceed \$3.6 million per year, which such limit will be reviewed on an annual basis. As of and for the year ended December 31, 2010, the Company was in compliance with these covenants.

Principal loan repayments over the next five years are as follows:

**Current portion:**

|      |              |
|------|--------------|
| 2011 | \$ 1,305,883 |
|------|--------------|

**8. Investment:**

Prior to November 2008, the Company held an interest in Afilius, Limited ("Afilius"), a private company, which provides complete back-office services for all registry management needs.

On November 4, 2008, Tucows (Delaware) Inc. ("Tucows DE"), a wholly owned subsidiary of the Company entered into a stock redemption agreement with Afilius Limited ("Afilius"), whereby Tucows DE agreed to sell its 353,722 Class A ordinary shares in Afilius to Afilius, for an amount of \$7,502,444, or \$21.21 per share, less one-half of the stamp duty amounting to \$37,513 required to be paid under Irish law.

The redemption of these shares was completed in three tranches as follows:

1.

In November 2008, the first closing, Afilius purchased a total of 153,722 shares of Class A ordinary shares of Afilius owned by Tucows DE for an aggregate purchase price of \$3,244,141, net of stamp duty.

2.

In April 2009, the second closing, Afilius purchased a total of 100,000 shares of Class A ordinary shares of Afilius owned by Tucows DE for an aggregate purchase price of \$2,110,395, net of stamp duty.

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**8. Investment: (Continued)**

3.

In September 2009, the third and final closing, Afilius purchased a total of 100,000 shares of Class A ordinary shares of Afilius owned by Tucows DE for an aggregate purchase price of \$1,980,000, net of stamp duty.

The Company received accelerated payments on the second and third tranches in exchange for aggregate consideration not exceeding 5% of the total proceeds of those tranches or 3% of the total consideration. The sale of the Afilius shares was accounted for in the periods in which they were sold.

**9. Common shares:**

The Company's authorized common share capital is 250 million common shares without nominal or par value. On December 31, 2010, there were 53,448,591 common shares outstanding.

Repurchase of common shares:

(a) Modified Dutch Tender Offers:

On March 23, 2009, the Company announced that it successfully concluded a modified "Dutch auction tender offer" that was previously announced on February 12, 2009. Under the terms of the offer, the Company repurchased an aggregate of 4,185,769 shares of its common stock at a purchase price of \$0.41 per share, for a total of \$1,716,132, excluding transaction costs of \$95,046. The purchase price was funded from available cash. Of the 4,185,769 shares purchased, 4,000,000 were shares the Company offered to purchase in the offer and 185,769 were shares purchased pursuant to the Company's right to purchase up to an additional 2% of the shares outstanding immediately prior to the commencement of the tender offer. Due to over-subscription, the final proration factor for shares tendered at or below \$0.41 per share was approximately 99.42%. For this purpose, shares tendered at \$0.41 per share included shares tendered by those persons who indicated, in their letter of transmittal, that they were willing to accept the price determined in the offer. All shares purchased in the tender offer received the same price. As a result of the completion of the tender offer, as of March 23, 2009, the Company had 68,888,092 shares issued and outstanding, as all shares repurchased were immediately retired.

On July 14, 2009 the Company announced that it successfully concluded a second modified Dutch auction tender offer that was previously announced May 26, 2009. Under the terms of the offer, the Company repurchased an aggregate of 1,103,824 shares of its common stock at a purchase price of \$0.45 per share, for a total of \$496,721, excluding transaction costs of \$73,614. The purchase price was funded from available cash. Of the 1,103,824 shares purchased, 1,000,000 were shares the Company offered to purchase in the offer and 103,824 were shares purchased pursuant to the Company's right to purchase up to an additional 2% of the shares outstanding immediately prior to the commencement of the tender offer. Due to over-subscription, the final proration factor for shares tendered at or below \$0.45 per share was approximately 99.82%. For this purpose, shares tendered at \$0.45 per share included shares tendered by those persons who indicated, in their letter of transmittal, that they were willing to accept the price determined in the offer. All shares purchased in the tender offer received the same price. As a result of the completion of the tender offer, as of July 14, 2009, the Company had 67,865,396 shares issued and outstanding, as all shares repurchased were immediately retired.

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**9. Common shares: (Continued)**

On October 2, 2009 the Company announced that it successfully concluded a third modified Dutch auction tender offer that was previously announced August 20, 2009. Under the terms of the offer, the Company repurchased an aggregate of 784,643 shares of its common stock at a purchase price of \$0.60 per share, for a total of \$470,786, excluding transaction costs of \$63,683. The purchase price was funded from available cash. All shares purchased in the tender offer received the same price. As a result of the completion of the tender offer, as of October 2, 2009, the Company had 67,080,453 shares issued and outstanding, as all shares repurchased were immediately retired.

On January 13, 2010, the Company announced that it successfully concluded a modified "Dutch auction tender offer" that was previously announced on December 14, 2009. Under the terms of the offer, the Company repurchased an aggregate of 6,341,470 shares of its common stock at a purchase price of \$0.70 per share, for a total of \$4,439,029, excluding transaction costs of \$51,957. The purchase price was funded from available cash. Of the 6,341,470 shares purchased, 5,000,000 were shares the Company offered to purchase in the offer and 1,341,470 were shares purchased pursuant to the Company's right to purchase up to an additional 2% of the shares outstanding immediately prior to the commencement of the tender offer. Due to over-subscription, the final proration factor for shares tendered at or below \$0.70 per share was approximately 99.9%. For this purpose, shares tendered at \$0.70 per share included shares tendered by those persons who indicated, in their letter of transmittal, that they were willing to accept the price determined in the offer. All shares purchased in the tender offer received the same price and all shares repurchased were immediately retired.

On October 13, 2010, the Company announced that it successfully concluded a modified Dutch auction tender offer that was previously announced September 17, 2010. Under the terms of the offer, the Company repurchased an aggregate of 3,913,570 shares of its common stock at a purchase price of \$0.70 per share, for a total of \$2,739,499, excluding transaction costs of \$52,802. The purchase price was funded from available cash. Of the 3,913,570 shares purchased, 2,900,000 were shares the Company offered to purchase in the offer and 1,013,570 were shares purchased pursuant to the Company's right to purchase up to an additional 2% of the shares outstanding immediately prior to the commencement of the tender offer. All shares purchased in the tender offer received the same price and all shares repurchased were immediately retired.

(b) Normal Course Issuer Bids:

In May 2008, our Board of Directors approved a stock buyback program, whereby during the period May 12, 2008 to May 11, 2009, the Company may repurchase up to 6,361,769 common shares of Tucows either through the facilities of the NYSE Amex or the Toronto Stock Exchange.

The common shares purchased under this program were cancelled. No shares were repurchased during the year ended December 31, 2009. For the year ended December 31, 2008, the Company repurchased a total of 849,760 common shares for \$272,444. A charge of \$102,492 was recorded in additional paid in capital for the excess of the purchase price over the carrying value of the common shares.

On February 16, 2010, the Company's Board of Directors authorized the repurchase of up to \$10 million of the Company's common stock at the Company's discretion under a normal course issuer bid ("NCIB"). The common shares purchased under this program were cancelled. The Company has repurchased 3,409,300 shares under this repurchase program during the year ended December 31, 2010.

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**Tucows Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**(Dollar Amounts in U.S. dollars)**

**9. Common shares: (Continued)**

A charge of \$1,741,947 was recorded in additional paid in capital for the excess of the purchase price over the carrying value of the common shares. The NCIB terminated upon the commencement of the modified Dutch Tender Offer described in the paragraph above.

**10. Stock option plans:**

The Company's 1996 Stock Option Plan was established for the benefit of the employees, officers, directors and certain consultants of the Company. The maximum number of common shares which may be set aside for issuance under the Plan was 11,150,000 shares, provided that the Board of Directors of the Company has the right, from time to time, to increase such number subject to the approval of the stockholders of the Company when required by law or regulatory authority. Generally, options issued under the Plan vest over a four-year period. The 1996 Compensation Equity Plan expired on February 25, 2006; no options were issued from this plan after that date.

On November 22, 2006, the Shareholders of the Company approved the Company's 2006 Equity Compensation Plan, which was amended and restated effective July 29, 2010 and which serves as a successor to the 1996 Stock Option Plan. The Company's 2006 Equity Compensation Plan has been established for the benefit of the employees, officers, directors and certain consultants of the Company. The maximum number of common shares which have been set aside for issuance under the Plan is 5.0 million shares. On October 8, 2010, the 2006 Equity Compensation Plan was amended to increase the number of shares which have been set aside for issuance by an additional 1.9 million shares to 6.9 million shares. Generally, options issued under the Plan vest over a four-year period and have a term not exceeding seven years, except for automatic formula grants of non-qualified stock options, which are immediately exercisable and have a five year term.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. Because option-pricing models require the use of subjective assumptions, changes in these assumptions can materially affect the fair value of the options. The assumptions presented in the table below represent the weighted average of the applicable assumption used to value stock options at their grant date. The Company calculates expected volatility based on historical volatility of the Company's common shares. The expected term, which represents the period of time that options granted are expected to be outstanding, is estimated based on historical exercise experience. The Company evaluated historical exercise behavior when determining the expected term assumptions. The risk-free rate assumed in valuing the options is based on the U.S. Treasury yield curve in effect at the time of grant for the expected term of the option. The Company determines the expected dividend yield percentage by dividing the expected annual dividend by the market price of Tucows Inc. common shares at the date of grant.

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## Tu cows Inc.

## Notes to Consolidated Financial Statements (Continued)

(Dollar Amounts in U.S. dollars)

## 10. Stock option plans: (Continued)

The fair value of stock options granted during the years ended December 31, 2010, 2009 and 2008 was estimated using the following assumptions:

|   | Year ended December 31, |         |         |
|---|-------------------------|---------|---------|
|   | 2010                    | 2009    | 2008    |
| Volatility  | 71.9%                   | 81.6%   | 65.5%   |
| Risk-free interest rate   | 1.9%                    | 1.2%    | 2.9%    |
| Expected life (in years)  | 4.4                     | 2.5     | 4.2     |
| Dividend yield  |                         | %       | %       |
| The weighted average grant date fair value for options issued, with the exercise price equal to market value on the date of grant | \$ 0.39                 | \$ 0.27 | \$ 0.31 |

Details of stock option transactions are as follows:

|                                  | Year ended<br>December 31, 2010 |   | Year ended<br>December 31, 2009 |   | Year ended<br>December 31, 2008 |   |
|----------------------------------|---------------------------------|---|---------------------------------|---|---------------------------------|---|
|                                  | Number of<br>shares             | Weighted<br>average<br>exercise<br>price<br>per share | Number of<br>shares             | Weighted<br>average<br>exercise<br>price<br>per share | Number of<br>shares             | Weighted<br>average<br>exercise<br>price<br>per share |
| Outstanding, beginning of year   | 7,213,977                       | \$ 0.56   | 7,292,777                       | \$ 0.51   | 6,249,517                       | \$ 0.56   |
| Granted                          | 1,804,000                       | 0.69  | 245,000                         | 0.54  | 1,276,000                       | 0.58  |
| Exercised                        | (33,678)                        | 0.44  | (68,707)                        | 0.37  | (35,000)                        | 0.27  |
| Forfeited                        | (204,959)                       | 0.66  | (213,593)                       | 0.59  | (192,740)                       | 0.73  |
| Expired                          | (507,091)                       | 1.02  | (41,500)                        | 0.80  | (5,000)                         | 0.27  |
| Outstanding, end of year         | 8,272,249                       | \$ 0.56   | 7,213,977                       | \$ 0.56   | 7,292,777                       | \$ 0.56   |
| Options exercisable, end of year | 6,205,248                       | \$ 0.51   | 6,088,342                       | \$ 0.53   | 5,629,735                       | \$ 0.51   |

The stock options expire at various dates through 2017.

As of December 31, 2010, the exercise prices, weighted average remaining contractual life of outstanding options and intrinsic values were as follows:

| Exercise price  | Number<br>outstanding | Options outstanding                                   |   | Aggregate<br>intrinsic<br>value | Number<br>exercisable | Options exercisable                                   |                                 |
|-----------------|-----------------------|---|---|---------------------------------|-----------------------|---|---------------------------------|
|                 |                       | Weighted<br>average<br>exercise<br>price<br>per share | Weighted<br>average<br>remaining<br>contractual<br>life (years) |                                 |                       | Weighted<br>average<br>exercise<br>price<br>per share | Aggregate<br>intrinsic<br>value |
| \$0.31 - \$0.49 | 3,684,295             | \$ 0.38   | 2.5   | \$ 1,282,081                    | 3,684,295             | \$ 0.38   | \$ 1,282,081                    |
| \$0.56 - \$0.69 | 1,942,454             | \$ 0.59   | 4.0   | 262,928                         | 1,545,954             | \$ 0.59   | 214,883                         |
| \$0.70 - \$0.99 | 2,645,500             | \$ 0.77   | 4.9   | 45,380                          | 975,000               | \$ 0.85   | 2,150                           |
|                 | 8,272,249             | \$ 0.56   |   | \$ 1,590,389                    | 6,205,249             | \$ 0.51   | \$ 1,499,114                    |



Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****10. Stock option plans: (Continued)**

Total unrecognized compensation cost relating to unvested stock options at December 31, 2010, prior to the consideration of expected forfeitures, is approximately \$597,000 and is expected to be recognized over a weighted average period of 3.6 years.

The total intrinsic value of options exercised during the years ended December 31, 2010, 2009 and 2008 was \$10,000, \$1,000 and \$12,000, respectively. Cash received from the exercise of stock options during the years ended December 31, 2010, 2009 and 2008 was \$14,809, \$25,422 and \$9,450 respectively.

The Company recorded stock-based compensation amounting to \$400,002, \$295,261 and \$287,800 for the years ended December 31, 2010, 2009 and 2008 respectively.

**11. Income taxes:**

The provision for income taxes differs from the amount computed by applying the statutory Federal income tax rate of 34% to the income before provision for income taxes as a result of the following:

|  | Year ended<br>December 31,<br>2010 | Year ended<br>December 31,<br>2009 | Year ended<br>December 31,<br>2008 |
|--|------------------------------------|------------------------------------|------------------------------------|
| Income for the year before provision for income taxes  | \$ 2,327,793                       | \$ 11,989,822                      | \$ 2,195,943                       |
| Computed expected tax expense  | \$ 791,450                         | \$ 4,076,539                       | \$ 768,580                         |
| Increase (reduction) in income tax expense resulting from:   |                                    |                                    |                                    |
| State income taxes   | 5,819                              | 29,975                             | 65,878                             |
| Permanent differences, including foreign exchange  | (22,812)                           | 800,535                            | 45,443                             |
| Investment tax credits recovered   | (50,311)                           | (281,320)                          |                                    |
| Other, including alternative minimum tax and adjustments to opening deferred tax assets            | 82,928                             | 864,950                            | (207,738)                          |
| Effect of change in income tax rates   |                                    | 772,093                            |                                    |
| Change in beginning of the year balance of the valuation allowance allocated to income tax expense | (596,229)                          | (6,514,156)                        | (551,029)                          |
| Provision for (recovery of) income taxes   | 210,845                            | \$ (251,384)                       | \$ 121,134                         |

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****11. Income taxes: (Continued)**

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets as of December 31, 2010 and 2009 are presented below:

|  | December 31,<br>2010  | December 31,<br>2009  |
|--|-----------------------|-----------------------|
| <b>Deferred tax assets:</b>                  |                       |                       |
| Net operating losses carried forward         | \$                    | \$                    |
| Deferred revenue                             | 5,732,912             | 5,513,843             |
| Amortization                                 | 2,077,758             | 2,644,932             |
| <b>Total gross deferred tax assets</b>       | <b>7,810,670</b>      | <b>8,158,775</b>      |
| Less valuation allowance                     | (3,655,070)           | (4,251,299)           |
| <b>Net deferred tax assets</b>               | <b>\$ 4,155,600</b>   | <b>\$ 3,907,476</b>   |
| Deferred income tax asset, current portion   | \$                    | \$                    |
| Deferred income tax asset, long-term portion | 4,155,600             | 3,907,476             |
|  | \$ 4,155,600          | \$ 3,907,476          |
| <b>Deferred tax liabilities:</b>             |                       |                       |
| Reserves and other                           | \$ (1,155,600)        | \$ (907,476)          |
| <b>Indefinite life intangible assets</b>     | <b>\$ (4,840,000)</b> | <b>\$ (4,840,000)</b> |

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the years in which those temporary differences become deductible. Management considers projected future taxable income, uncertainties related to the industry in which the Company operates, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods which the deferred tax assets are deductible, management believes it is appropriate to record a valuation allowance in the amount of \$3.7 million at December 31, 2010 and a valuation allowance in the amount of \$4.3 million at December 31, 2009.

At December 31, 2010 Tucows' unrecognized tax benefits amounted to \$167,000, which if recognized would favorably affect the income tax rate in future periods. The increase from the prior year amount of \$124,000 relates to an unrecognized tax benefit for 2010 research and development tax credits offset by settlement of certain amounts in Pennsylvania related to the 1996 - 2000 taxation years net of adjustments to certain amounts related to subsequent years.

The Company recognizes accrued interest and penalties related to unrecognized tax benefit in tax expense. The Company did not have any significant interest and penalties accrued as of January 1, 2009 and December 31, 2010.

Tucows believes that it is reasonably possible that \$117,000 of the unrecognized tax benefit will decrease in the next twelve months as it is anticipated that the U.S. tax authorities will finalize their review of prior years' taxes owing in Pennsylvania within that period and that certain other state tax returns will be filed.





Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****11. Income taxes: (Continued)**

The following is a reconciliation of Tucows's change in uncertain tax position under FIN 48:

|   | <b>Total Gross<br/>Unrecognized<br/>Tax Benefits</b> |
|---|--|
| Balance as at December 31, 2009                         | \$ 124,000   |
| Increase in uncertain tax benefits for the current year | 50,000   |
| Decrease in uncertain tax benefits of prior years       | (7,000)  |
| Balance as at December 31, 2010                         | \$ 167,000   |

**12. Other income, net:**

In connection with the sale of the Company's investment in Afiliis, the Company recognized a gain on disposition of the first tranche of shares in the amount of \$3.1 million during Fiscal 2008. During Fiscal 2009, the Company recognized gains on disposition of the second and third and final share tranches of \$2.0 million and \$1.9 million, respectively.

Afiliis has also paid dividends aggregating to \$454,000 in Fiscal 2008. These dividends have been recorded as other income in the statement of operations. No dividends were paid during Fiscal 2010 and Fiscal 2009.

In 2002, we assigned to an unrelated third party, various patents which were acquired by us in the merger with Infonautics in 2001. In connection with the assignment of these patents, we retained the right to a share of any cash flow received by the unrelated third party relating to the commercialization of these patents. As a result of this assignment, during the year ended December 31, 2009 we received an amount of \$603,000. No amount was received during the year ended December 31, 2010 as a result of this assignment. During the year ended December 31, 2008 we received an amount of \$235,000.

As part of the Company's decision to divest of non-strategic assets, in June and September 2008 the Company entered into definitive agreements with two purchasers to acquire the Company's web hosting end-user websites and customers. This resulted in our recording a gain on the sale of these customer relationships of \$2.1 million during Fiscal 2008.

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****13. Earnings per common share:**

The following table reconciles the numerators and denominators of the basic and diluted earnings per common share computation:

|  | Year ended<br>December 31,<br>2010 | Year ended<br>December 31,<br>2009 | Year ended<br>December 31,<br>2008 |
|--|------------------------------------|------------------------------------|------------------------------------|
| Numerator for basic and diluted earnings per common share:   |                                    |                                    |                                    |
| Income for the year  | \$ 2,116,948                       | \$ 12,241,206                      | \$ 2,074,809                       |
| Denominator for basic and diluted earnings per common share: |                                    |                                    |                                    |
| Basic weighted average number of common shares outstanding   | 57,982,248                         | 69,145,001                         | 73,817,347                         |
| Effect of stock options                                      | 1,973,540                          | 1,211,012                          | 1,012,870                          |
| Diluted weighted average number of shares outstanding        | 59,955,788                         | 70,356,013                         | 74,830,217                         |
| Basic earnings per common share                              | \$ 0.04                            | \$ 0.18                            | \$ 0.03                            |
| Diluted earnings per common share                            | \$ 0.04                            | \$ 0.17                            | \$ 0.03                            |

Options to purchase 2,937,000 common shares were outstanding during 2010 (2009: 3,780,962; 2008: 3,123,980) but were not included in the computation of diluted income per common share because the options' exercise price was greater than the average market price of the common shares. The options which expire in years 2011 to 2017 were still outstanding at the end of 2010.

**14. Commitments and contingencies:**

(a) The Company has several non-cancelable lease and purchase obligations primarily for general office facilities and equipment that expire over the next ten years. Future minimum payments under these agreements are as follows:

|            |              |
|------------|--------------|
| 2011       | \$ 2,068,000 |
| 2012       | 1,506,000    |
| 2013       | 675,000      |
| 2014       | 474,000      |
| 2015       | 474,000      |
| Thereafter | 2,640,000    |

Rental expense under operating lease agreements was \$593,000, \$540,000, and \$563,000 for the years ended December 31, 2010, 2009 and 2008 respectively.

(b) In the normal course of its operations, the Company becomes involved in various legal claims and lawsuits. The Company intends to vigorously defend these claims. While the final outcome with respect to any actions outstanding or pending as at December 31, 2010 cannot be predicted with

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****14. Commitments and contingencies: (Continued)**

certainly, it is the opinion of management that their resolution will not have a material adverse effect on the Company's financial position.

**15. Fair value measurement:**

For financial assets and liabilities recorded in our financial statements at fair value we utilize a valuation hierarchy for disclosure of the inputs to valuation used to measure fair value. This hierarchy prioritizes the inputs into three broad levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument. Level 3 inputs are unobservable inputs based on the Company's own assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The following table provides a summary of the fair values of the Company's derivative instruments measured at fair value on a recurring basis as at December 31, 2010:

**December 31, 2010**

|                             | Fair Value Measurements Using |            |         | Assets at<br>Fair Value |
|-----------------------------|-------------------------------|------------|---------|-------------------------|
|                             | Level 1                       | Level 2    | Level 3 |                         |
| Derivative instrument asset | \$                            | \$ 833,960 | \$      | \$ 833,960              |
| Total Assets                | \$                            | \$ 833,960 | \$      | \$ 833,960              |

The following table provides a summary of the fair values of the Company's derivative instruments measured at fair value on a recurring basis as at December 31, 2009:

**December 31, 2009**

|                             | Fair Value Measurements Using |              |         | Liabilities at<br>Fair Value |
|-----------------------------|-------------------------------|--------------|---------|------------------------------|
|                             | Level 1                       | Level 2      | Level 3 |                              |
| Derivative instrument asset | \$                            | \$ 2,204,670 | \$      | \$ 2,204,670                 |
| Total Assets                | \$                            | \$ 2,204,670 | \$      | \$ 2,204,670                 |

**16. Subsequent events:**

In March 2011 the Company received notification that it had earned an additional amount of \$0.3 million as a result of a routine audit in connection with Infonautics patents that it assigned in 2002 to a third party who continues to commercialize these patents. The Company expects payment of this amount imminently. In connection with the assignment of these patents, the Company retained the right to share in certain revenue relating to any cash flow received by such third party. This revenue is comparable to the \$0.6 million the Company recognized in June 2009 in connection with these patents. As the costs of commercializing the patents are expected to increase in the future, the Company does not expect any future revenue received to be material.



Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****17. Supplemental information:**

(a) The following is a summary of the Company's revenue earned from each significant revenue stream:

|                        | Year ended December 31, |               |               |
|------------------------|-------------------------|---------------|---------------|
|                        | 2010                    | 2009          | 2008          |
| OpenSRS:               |                         |               |               |
| Domain Services        | \$ 64,977,121           | \$ 59,248,732 | \$ 53,966,640 |
| Email Services         | 2,325,253               | 3,636,866     | 5,765,223     |
| Other Services         | 4,368,781               | 4,425,940     | 4,476,676     |
| Total OpenSRS Services | 71,671,155              | 67,311,538    | 64,208,539    |
| Yummy Names            | 6,123,708               | 6,623,292     | 4,896,943     |
| Hover                  | 4,559,833               | 4,970,635     | 7,194,352     |
| Butterscotch           | 2,223,809               | 2,033,747     | 2,168,046     |
|                        | \$ 84,578,505           | \$ 80,939,212 | \$ 78,467,880 |

During the years ended December 31, 2010, 2009 and 2008, no customer accounted for more than 10% of total revenue. As at December 31, 2010, three customers accounted for 35% of accounts receivable, as at December 31, 2009, one customer accounted for 11% of accounts receivable, while as at December 31, 2008, two customers accounted for 20% of accounts receivable.

(b) The following is a summary of the Company's cost of revenues from each significant revenue stream:

|  | Year ended December 31, |               |               |
|--|-------------------------|---------------|---------------|
|  | 2010                    | 2009          | 2008          |
| OpenSRS:                                     |                         |               |               |
| Domain Services                              | \$ 54,087,893           | \$ 48,202,033 | \$ 42,854,184 |
| Email Services                               | 425,836                 | 546,455       | 340,048       |
| Other Services                               | 1,570,481               | 1,622,086     | 1,629,894     |
| Total OpenSRS Services                       | 56,084,210              | 50,370,574    | 44,824,126    |
| Yummy Names                                  | 817,290                 | 847,269       | 716,627       |
| Hover  | 1,527,727               | 1,925,188     | 2,272,532     |
| Butterscotch                                 | 65,622                  | 44,886        | 29,195        |
| Network, other costs                         | 4,648,899               | 4,748,189     | 6,771,556     |
| Network, depreciation and amortization costs | 1,331,576               | 1,789,987     | 3,073,649     |
|  | \$ 64,475,324           | \$ 59,726,093 | \$ 57,687,685 |

Table of Contents**Tucows Inc.****Notes to Consolidated Financial Statements (Continued)****(Dollar Amounts in U.S. dollars)****17. Supplemental information: (Continued)**

(c) The following is a summary of the Company's property and equipment by geographic region:

|                | Year ended December 31, |              |              |
|----------------|-------------------------|--------------|--------------|
|                | 2010                    | 2009         | 2008         |
| Canada         | \$ 1,041,692            | \$ 1,475,056 | \$ 2,292,358 |
| United States  | 510,657                 | 506,533      | 752,274      |
| United Kingdom |                         | 5,179        | 28,326       |
|                | \$ 1,552,349            | \$ 1,986,768 | \$ 3,072,958 |

(d) The following is a summary of the Company's amortizable intangible assets by geographic region:

|               | Year ended December 31, |              |              |
|---------------|-------------------------|--------------|--------------|
|               | 2010                    | 2009         | 2008         |
| Canada        | \$ 2,621,160            | \$ 4,189,728 | \$ 5,575,884 |
| United States | 57,600                  | 230,400      | 403,200      |
|               | \$ 2,678,760            | \$ 4,420,128 | \$ 5,979,084 |

(e) The following is a summary of the Company's deferred tax asset, net of valuation allowance, by geographic region:

|        | Year ended December 31, |              |              |
|--------|-------------------------|--------------|--------------|
|        | 2010                    | 2009         | 2008         |
| Canada | \$ 4,155,600            | \$ 3,907,476 | \$ 3,000,000 |
|        | \$ 4,155,600            | \$ 3,907,476 | \$ 3,000,000 |

(f) Valuation and qualifying accounts:

|   | Balance at<br>beginning year | Charged to<br>(recovered)<br>costs and<br>expenses | Write-offs<br>during year | Balance at<br>end of year |
|---|------------------------------|--|---------------------------|---------------------------|
| Allowance for doubtful accounts, including provision for credit notes |                              |  |                           |                           |
| 2010  | \$ 115,000                   | \$ (50,000)  | \$                        | \$ 65,000                 |
| 2009  | \$ 125,000                   | \$ (10,000)  | \$                        | \$ 115,000                |
| 2008  | \$ 95,000                    | \$ 30,000  | \$                        | \$ 125,000                |
| Valuation allowance for deferred tax asset:                           |                              |  |                           |                           |
| 2010  | \$ 4,251,000                 | \$ (595,930)                                       | \$                        | \$ 3,655,070              |

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|      |    |            |    |             |    |            |
|------|----|------------|----|-------------|----|------------|
| 2009 | \$ | 10,765,000 | \$ | (6,514,000) | \$ | 4,251,000  |
| 2008 | \$ | 11,316,000 | \$ | (551,000)   | \$ | 10,765,000 |

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**EXHIBIT INDEX**

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 3.1                | Fourth Amended and Restated Articles of Incorporation of Tucows Inc. (Incorporated by reference to Exhibit 3.1 filed with Tucows' current report on Form 8-K, as filed with the SEC on November 29, 2007).   |
| 3.2                | Second Amended and Restated Bylaws of Tucows Inc. (Incorporated by reference to Exhibit 3.2 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2006, as filed with the SEC on March 29, 2007).  |
| 10.1*              | 2006 Equity Compensation Plan, as amended and restated effective as of July 29, 2010 (Incorporated by reference to Exhibit 99(d)(1) filed with Tucows' Schedule TO, as filed with the SEC on September 17, 2010).  |
| 10.2*              | Employment Agreement dated January 22, 2003 between Tucows.com Co. and Elliot Noss (Incorporated by reference to Exhibit 10.5 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2003, as filed with the SEC on March 28, 2004).  |
| 10.3*              | Employment Agreement dated March 11, 2003 between Tucows.com Co. and Michael Cooperman (Incorporated by reference to Exhibit 10.5 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2003, as filed with the SEC on March 28, 2004).  |
| 10.4               | Lease between 707932 Ontario Limited and Tucows International Corporation, dated December 10, 1999 (Incorporated by reference to exhibit number 10.9 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2001, as filed with the SEC on April 1, 2002).  |
| 10.5               | Lease extension between 707932 Ontario Limited and Tucows Inc. and Tucows.com Co., dated September 4, 2004 (Incorporated by reference to Exhibit 10.5 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2004, as filed with the SEC on March 24, 2005).  |
| 10.6*              | Description of Tucows Fiscal 2004 At Risk Compensation Plan (Incorporated by reference to Exhibit 10.9 filed with Tucows' annual report on Form 10-K for the year ended December 31, 2004, as filed with the SEC on March 24, 2005).   |
| 10.7#              | Registrar Accreditation Agreement, effective as of June 25, 2005, as amended June 22, 2009, by and between the Internet Corporation for Assigned Names and Numbers and Tucows.com Co.  |
| 10.8               | Registry-Registrar Agreement, dated as of October 4, 2001, by and between VeriSign, Inc. and Tucows Inc. (Incorporated by reference to Exhibit 10.13 filed with Amendment No. 1 to Tucows' registration statement on Form S-1 (Registration No. 333-125843), as filed with the SEC on July 7, 2005).                                       |
| 10.11              | Loan Agreement, dated as of June 25, 2007, by and among Tucows.com Co., Tucows (Delaware) Inc., Tucows Inc., Mailbank Nova Scotia Co., Tucows Domain Holdings Co., Innerwise, Inc. and Bank of Montreal (Incorporated by reference to Exhibit 10.1 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007). |
| 10.12              | Guaranty, dated July 25, 2007, by Tucows Inc. in favor of Bank of Montreal (Incorporated by reference to Exhibit 10.2 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007).  |
| 10.13              | Security Agreement, dated July 25, 2007, by Tucows Inc. in favor of Bank of Montreal (Incorporated by reference to Exhibit 10.3 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007).  |

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| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 10.14              | Financing Commitment, dated July 19, 2007, by and between Tucows.com Co. and Bank of Montreal (Incorporated by reference to Exhibit 10.3 filed with Tucows' current report on Form 8-K, as filed with the SEC on July 31, 2007).             |
| 10.15              | Operating Loan Agreement, dated September 10, 2010, between Tucows.com Co. and the Bank of Montreal. (Incorporated by reference to Exhibit 10.1 filed with Tucows' current report on Form 8-K, as filed with the SEC on September 13, 2010). |
| 10.16              | Offer Letter, dated August 30, 2010, between Tucows Inc. and the Bank of Montreal. (Incorporated by reference to Exhibit 10.2 filed with Tucows' current report on Form 8-K, as filed with the SEC on September 13, 2010).                   |
| 21.1#              | Subsidiaries of Tucows Inc.  |
| 23.1#              | Consent of KPMG LLP, Independent Registered Public Accounting Firm.  |
| 31.1#              | Chief Executive Officer's Rule 13a-14(a)/15d-14(a) Certification.  |
| 31.2#              | Chief Financial Officer's Rule 13a-14(a)/15d-14(a) Certification.  |
| 32.1#              | Chief Executive Officer's Section 1350 Certification.  |
| 32.2#              | Chief Financial Officer's Section 1350 Certification.  |

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\*

Management or compensatory contract required to be filed pursuant to Item 15(c) of the requirements for Form 10-K reports.

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Filed herewith.

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Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**TUCOWS INC.**

By: /s/ ELLIOT NOSS

Name: Elliot Noss

Title: *Chief Executive Officer and President*

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

| Signature   | Title   | Date           |
|---|---|----------------|
| <u>/s/ ELLIOT NOSS</u><br>Elliot Noss               | President, Chief Executive Officer (Principal Executive Officer) and Director | March 22, 2011 |
| <u>/s/ MICHAEL COOPERMAN</u><br>Michael Cooperman   | Chief Financial Officer (Principal Financial and Accounting Officer)          | March 22, 2011 |
| <u>/s/ STANLEY STERN</u><br>Stanley Stern           | Director  | March 22, 2011 |
| <u>/s/ EUGENE FIUME</u><br>Eugene Fiume             | Director  | March 22, 2011 |
| <u>/s/ EREZ GISSIN</u><br>Erez Gissin               | Director  | March 22, 2011 |
| <u>/s/ JOICHI ITO</u><br>Joichi Ito                 | Director  | March 22, 2011 |
| <u>/s/ ALLEN KARP</u><br>Allen Karp                 | Director  | March 22, 2011 |
| <u>/s/ LLOYD N. MORRISETT</u><br>Lloyd N. Morrisett | Director  | March 22, 2011 |

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| <b>Signature</b>                                      | <b>Title</b> | <b>Date</b>    |
|---|--------------|----------------|
| <hr/> <i>/s/ RAWLEIGH RALLS</i><br>Rawleigh Ralls     | Director     | March 22, 2011 |
| <hr/> <i>/s/ JEFFREY SCHWARTZ</i><br>Jeffrey Schwartz | Director     | March 22, 2011 |
| <hr/>   |              |                |