

CRYPTOLOGIC LTD  
Form 20-F  
March 31, 2010

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

**FORM 20-F**

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

OR

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
**For the fiscal year ended December 31, 2009**

OR

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

OR

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

Commission file number **0-30224**

**CryptoLogic Limited**

(Exact name of Registrant as specified in its charter)

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**Guernsey, Channel Islands**

(Jurisdiction of incorporation or organization)

**Marine House, Clanwilliam Place**

**Dublin 2**

**Ireland**

(Address of principal executive offices)

**Stephen Taylor**

**Marine House, Clanwilliam Place**

**Dublin 2**

**Ireland**

**Tel: +353 1 234 0400 Fax: +353 1 661-9637**

(Name, telephone, e-mail and/or facsimile number and address of contact person)

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

Title of each class:	Name of each exchange on which registered:
<b>Common Shares</b>	<b>NASDAQ Global Select Market</b>

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

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

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of December 31, 2009.

**13,819,051 Common Shares (including 1,025,031 Exchangeable Shares)**

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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-Accelerated Filer

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

U.S. GAAP

International Financial Reporting Standards as issued by the International Accounting Standards Board

Other

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

Item 17

Item 18

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If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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### Presentation of Financial and Other Information

In this annual report, except as otherwise indicated or as the context otherwise requires, the Company, we, us and our refers to CryptoLogic Limited and its operating subsidiaries.

Pursuant to a business reorganization implemented by way of an Ontario, Canada Superior Court of Justice court approved plan of arrangement (the Arrangement) and approved by the shareholders on May 24, 2007, CryptoLogic Limited acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement became an indirect subsidiary of CryptoLogic Limited. As part of the Arrangement, the Company issued either an equivalent amount of CryptoLogic Limited common shares (Common Shares) or, in the case of taxable Canadian residents, exchangeable shares (Exchangeable Shares) of CryptoLogic Exchange Corporation (CEC), an indirect subsidiary of CryptoLogic Limited. The Exchangeable Shares are, as nearly as practicable, the economic equivalent of the Common Shares. The holders of Exchangeable Shares and Common Shares participate equally in voting and dividends. No additional shares of CEC have been or will be issued.

For accounting purposes, the Arrangement has been accounted for using the continuity of interest method, which recognizes CryptoLogic Limited as the successor entity to CryptoLogic Inc. Accordingly, financial information presented in the annual report reflects the financial position, results of operations and cash flows as if CryptoLogic Limited has always carried on the business formerly carried on by CryptoLogic Inc., with all assets and liabilities recorded at the carrying values of CryptoLogic Inc. The interest held by CEC shareholders has been presented as a minority interest in the consolidated financial statements, as required under Canadian generally accepted accounting principles (Canadian GAAP).

We have prepared our financial statements in accordance with Canadian GAAP, which are different from generally accepted accounting principles in the United States (U.S. GAAP) and may not be comparable to financial statements of United States companies. Significant measurement differences in our financial information between Canadian GAAP and U.S. GAAP for the years ended December 31, 2009, 2008, and 2007 are disclosed in Note 21 to our audited consolidated financial statements.

In this annual report, all currency refers to U.S. Dollars (US\$) and all information is as of March 11, 2010 unless indicated otherwise.

Percentages and some amounts in this annual report have been rounded for ease of presentation. Any discrepancies between totals and the sums of the amounts listed are due to rounding.

Information contained in this annual report concerning the industry in which we operate has been obtained from publicly available information from third party sources (including Global Betting and Gaming Consultants, March 2009, or GBGC). Although we believe such information is reliable, we have not had such information verified by any independent source.

This annual report contains trade names, trademarks, registered marks, and service marks including DC Comics, Superman, Wonder Woman, Marvel, Jenga, Batman, Spider-Man and The Hulk belonging to us and other companies. All trademarks, trade names, registered marks, and service marks appearing in this annual report are the property of their respective holders.



Cautionary Statement Regarding Forward-Looking Information

This annual report contains forward-looking statements within the meaning of Section 27A of the U.S. Securities Act of 1933, as amended, and Section 21E of the U.S. Securities Exchange Act of 1934, as amended, adopted pursuant to the Private Securities Litigation Reform Act of 1995. Statements that are not purely historical may be forward-looking, including statements regarding our expectations, objectives, anticipations, estimations, intentions, plans, hopes, beliefs, or strategies regarding the future. Such forward-looking statements include, but are not limited to:

the financial or business impact of new or amendments to legislation or regulation in individual countries or by multi-jurisdictional governmental organizations;  
the impact of the loss of key licensees;

the impact of recent new customers and expected additional customers to partially offset revenue lost from William Hill;

the success of our new growth strategy and restructuring program to reduce operating costs and return to profitability and positive cash flow;  
expected revenue growth from branded games and hosted casino licensing in 2010;

potential new revenue sources in 2010 from gaming sites;

the increased liquidity and profitability (albeit at lower levels), and lower costs, resulting from outsourcing of our poker network;

the impact of potential legal proceedings upon our business; and

statements that include the words may, will, plans, estimates, anticipates, believes, expects, intends and other similar

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Achievement of future results is subject to risks, uncertainties, and potentially inaccurate assumptions. These risks and uncertainties include, among others, those discussed in Item 3. Key Information-Risk Factors of this annual report, (including without limitation, risks associated with i) existing and potential future changes to government regulation, ii) the current global financial condition, iii) legal proceedings, iv) foreign exchange fluctuations, and v) competition) as well as our consolidated financial statements, related Notes, and the other financial information appearing elsewhere in this annual report and our other documents we file with or furnish to the Securities and Exchange Commission. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could differ materially from past results and those anticipated, estimated or projected. You should bear this in mind as you consider forward-looking statements. We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events, or otherwise.

**PART I****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not Applicable.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not Applicable.

**ITEM 3. KEY INFORMATION****SELECTED FINANCIAL DATA**

The following financial information of our Company, expressed in U.S. dollars unless otherwise indicated, is only a summary and should be read in conjunction with, and is qualified in its entirety by reference to, our audited annual consolidated financial statements and the related notes, which are included in this annual report. The selected historical financial data set forth below as of and for each of the years ended indicated has been derived from our consolidated financial statements.

<b>For the Years Ended December 31,</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
<i>(In thousands, except per share disclosure)</i>					
Revenue	\$ 39,794	\$ 61,526	\$ 73,659	\$ 104,022	\$ 86,307
Net (loss)/earnings and comprehensive (loss)/income	\$ (35,510)	\$ (32,738)	\$ 5,528	\$ 24,812	\$ 20,530
Basic (loss)/earnings per share	\$ (2.78)	\$ (2.55)	\$ 0.47	\$ 1.83	\$ 1.51
Diluted (loss)/earnings per share	\$ (2.78)	\$ (2.55)	\$ 0.47	\$ 1.81	\$ 1.46
Basic weighted average number of shares	\$ 13,820	\$ 13,888	\$ 13,891	\$ 13,558	\$ 13,588
Diluted weighted average number of shares	\$ 13,820	\$ 13,888	\$ 13,907	\$ 13,731	\$ 14,067
Total assets	\$ 63,370	\$ 105,806	\$ 170,633	\$ 184,520	\$ 154,398
Shareholders' equity	\$ 36,796	\$ 72,440	\$ 109,306	\$ 111,584	\$ 87,225
Share capital	\$ 33,916	\$ 33,552	\$ 33,407	\$ 29,096	\$ 25,171
Dividends per share	\$ 0.07	\$ 0.39	\$ 0.48	\$ 0.43	\$ 0.22

Our financial statements have been prepared in accordance with Canadian GAAP. The significant measurement differences between Canadian GAAP and U.S. GAAP are described in Note 21 to the consolidated financial statements in respect of each of the years presented. If the Company had followed U.S. GAAP, certain items in the consolidated financial statements would have been reported as follow:

<b>For the Years Ended December 31,</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
<i>(In thousands, except per share disclosure)</i>					
Net (loss)/earnings	\$ (36,669)	\$ (33,048)	\$ 5,640	\$ 25,636	\$ 20,530
Basic (loss)/earnings per share	\$ (2.87)	\$ (2.57)	\$ 0.48	\$ 1.89	\$ 1.51

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Diluted (loss)/earnings per share	\$ (2.87)	\$ (2.57)	\$ 0.48	\$ 1.87	\$ 1.46
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**RISK FACTORS**

*Current and future legislation and court decisions may have a material impact on our operations and financial results*

The Company and our licensees are subject to applicable laws in the jurisdictions in which they operate. Our hosted casino licensees hold government licenses to operate Internet gaming sites hosted in Malta and our branded games licensees hold similar licenses issued by the jurisdictions in which their gaming servers are hosted. Some countries have introduced regulations attempting to restrict or prohibit Internet gaming, while others have taken the position that Internet gaming should be regulated and have adopted or are in the process of considering legislation to enable that regulation.

While the U.K. and other European countries such as Malta and Gibraltar have currently adopted a regime which permits its licensees to accept wagers from any jurisdiction, other countries, including Italy and France have, or are in the process of implementing regimes which only permit the targeting of the domestic market provided a local license is obtained and local taxes accounted for. Other European territories continue to defend a licensing regime that protects monopoly providers and have combined this with an attempt to outlaw all other supplies. Either of these restrictive approaches may yet be deemed to be in potential conflict (in any specific jurisdiction) with E.U. treaty law (governing the free movement of trade and services throughout the European Union) and case law rendered by the European Court of Justice (the ECJ). Over the past several years, the European Commission (the EC) has attempted to prompt the introduction of directives that would harmonize online gaming within the E.U., which is in line with the EC's stated goal of encouraging a free and open cross-border market, but this has met with substantial opposition. There is therefore no indication that any such harmonization will be achieved in the near term. Contemporaneous with its efforts to harmonize European online gaming laws, the EC has initiated infringement proceedings against various member states in relation to perceived breaches of Article 56 of the Treaty on the Functionality of the European Union (which article enshrines the principle of freedom of movement of services), but in most cases these have not reached conclusion.

As companies and consumers involved in Internet gaming are located around the globe, including our licensees and their players, there is uncertainty regarding which government has authority to regulate or legislate the industry. The Unlawful Internet Gaming Enforcement Act (UIGEA), which is designed to prohibit payments relating to Internet gaming was enacted on October 13, 2006 in the United States, and may be adopted in other jurisdictions.

Future legislative and court decisions may have a material impact on our operations and financial results. There is a risk that governmental authorities may view us or our licensees as having violated their local laws, despite CryptoLogic's contractual requirement that each of its licensees is licensed to operate an Internet gaming business by the governmental authority of the country in which the gaming servers associated with the licensees' gaming operations are located. Therefore, there is a risk that civil and criminal proceedings, including class actions brought by or on behalf of prosecutors or public entities incumbent monopoly providers, or private individuals, could be initiated against us, our licensees, Internet service providers, credit card processors, advertisers and others involved in the Internet gaming industry. Such potential proceedings could involve substantial litigation expense, penalties, fines, seizure of assets, injunctions or other restrictions being imposed upon us or our licensees or other business partners, while diverting the attention of key executives. Such proceedings could have a material adverse effect on our business, revenues, operating results and financial condition as well as impact upon our reputation.

There can be no assurance that legally enforceable prohibiting legislation will not be proposed and passed in jurisdictions relevant or potentially relevant to our business to legislate or regulate various aspects of the Internet or the Internet gaming industry (or that existing laws in those jurisdictions will not be interpreted negatively). Compliance with any such legislation may have a material adverse effect on our business, financial condition and results of operations, either as a result of our determining that a jurisdiction should be blocked, or because a local license may be costly for us or our licensees to obtain and/or such licenses may contain other commercially undesirable conditions.

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There have recently been a number of legal developments associated with the manner in which the business of gaming, and in particular, Internet gaming, is treated in the U.K. and Continental Europe. Some of these developments can be considered as positive and some as negative. In this regard a brief summary of the regulatory situation in the U.K., Europe, and the United States follows:

### United Kingdom

In September 2007, the U.K. Gambling Act came into force, which regulated online gaming for the first time in that jurisdiction. Most of the underlying codes in relation to entities established in the U.K., or marketing into the U.K. have been enacted. However, there is no assurance that the U.K. regulatory regime as interpreted by the Gambling Commission, the Gambling Act's independent regulator, will provide a commercially-viable market and may create restrictions that would have a material adverse effect on CryptoLogic's customers, business, revenues, operating results and/or financial condition. Indeed, the Department of Culture Media and Sport (the "DCMS") (the government body with responsibility for overseeing gambling), has recently announced that it may reconsider one of the main tenets of the Gambling Act, namely that if an online gaming operator was regulated either in Europe or in a jurisdiction approved by the DCMS (the so called "white listed jurisdictions") such an operator could fully target the UK gambling market. It seems likely that the DCMS will recommend (in a report to be published imminently) that it will require entities not licensed in the UK to acquire some form of additional accreditation to access the UK market and/or pay taxes in the UK.

### Continental Europe

#### France

France has decided to license the Internet gambling sector in 2010 but only in relation to poker games and sportsbook currently. It is therefore anticipated that the previously aggressive enforcement stance adopted by the French authorities is likely to resume when this regime is in force against those operators that fail to obtain any local license. Moreover, the licenses look likely to be subject to undesirable commercial terms, such as limits on maximum payouts and high levels of tax. Moreover, all poker play can only be amongst French customers, which will severely impede liquidity.

#### Germany

Online gambling was expressly prohibited in Germany by the State Gambling Treaty of 2008, under which an operator is liable to civil or administrative sanctions. Article 284 of the German Criminal Code which applies criminal sanctions to operators who provide online gambling services into Germany without a form of authorization has been the subject of legal debate over the purported breadth of its application.

Conflicting domestic court decisions on the legality of domestic law relating to online gambling (in light of the uncertainty of the application of Article 284 of the Criminal Code to online gambling businesses licensed outside of Germany, in particular by other EU member states, and the legality of the State Gambling Treaty under EU law) has led to uncoordinated enforcement action.

Moreover, the State Gambling Treaty expires on 31 December 2011, requiring Germany to address the issue of online gambling prior to this date. It may elect to adopt a similar regime to that implemented in France.

#### Italy

Recent willingness by the Italian government to regulate certain forms of Internet gaming could be perceived as indicative of a liberalization of the Internet gaming industry as a whole in that country. However, at present, the form of regulation put forward has failed to create attractive market conditions for many operators. As such, notwithstanding the fact that this market may appear to be liberalizing, in practice, Italy has not liberalized in a manner, or to a degree, that is helpful to the Company or its licensees. The Company and its licensees remain at

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risk that Italy may take aggressive action against parties whose operations are not licensed pursuant to the regulatory regimes established by this country and furthermore, the fact that some Internet gaming activity is permitted under license may be sufficient for Italy to resist any residual criticisms or enforcement initiatives by the EC.

### Spain

Madrid's and Basque's regional governments have recently implemented new legislation to regulate Internet gaming but it only permits services to be supplied by the licensed entity to Madrid residents. Therefore obtaining a license may be of little commercial value to any operator. Other regions may follow suit.

### Holland

CryptoLogic's licensees presently accept wagers from the Dutch market. The Dutch government has consistently taken steps to support and protect its state-sponsored casino operator's (Holland Casino) monopoly, including taking legal action against Internet gaming operators. In addition, an announcement in 2009 by the Dutch Minister of Justice to the effect that payment support by Dutch banks of online gaming was unlawful (and precluded by existing law) caused a number of operators to block from the territory, and this cautious approach has been further exacerbated by the negative (recently published) opinion of Advocate General Bot in the case referred to the ECJ by Betfair and Ladbrokes which sought in effect to challenge the Dutch monopoly (the court normally follows the Advocate General's opinion). In the event that the Dutch government seeks to take further steps to protect the online business of Holland Casino by discouraging other operators from operating in the Dutch marketplace, either through changes in legislation or enforcement measures, the Company's licensees (and CryptoLogic accordingly) could be adversely impacted.

### Scandinavia

Governments in most Scandinavian countries have attempted to discourage their citizens from gambling with online operators by taxing their citizens' winnings. Generally speaking, winnings realized through a state sponsored operator are not taxable, but winnings from other sources can be subject to inconsistent application of taxation law in relation to domestic and non-domestic products in the E.U. Until such time as the tax authorities in the various countries make an official pronouncement on the manner in which these tax laws will be applied, it is unclear as to what impact these tax policies will have on the business of the Company's licensees. In Norway, the government has specifically banned payment support of online gambling which came into force in 2010. The ban, means only payment support of state-owned gambling services will remain legal. In Denmark, the state monopoly on online gambling is being reconsidered by Danish government in light of EC criticism.

### United States

Since the enactment of UIGEA in October 2006, the Company has prohibited its licensees from taking any wagers from U.S. residents. The UIGEA sought to clarify the illegality of processing or transferring any funds connected with unlawful Internet gaming, although some U.S. enforcement agencies claimed that previous existing legislation similarly outlawed these activities. Given that the Company had previously derived licensing revenue and provided payment processing solutions (through its e-cash services) on behalf of some licensees who took wagers from the U.S., there is no guarantee that the U.S. Department of Justice will not seek to prosecute the Company, its officers or directors for alleged historic transgressions or similarly prosecute its licensees or their directors or shareholders. Such proceedings could result in criminal penalties, substantial fines, damages and sequestration of assets. They also could damage the reputation of the Company, divert the attention of the Company's key executives and have a material adverse effect on the business, revenues, operating results and/or financial condition of the Company.

***The loss of a major payment option could limit our ability to accept deposits.***

With the enactment of the UIGEA, financial institutions in the United States ceased to accept online gaming transactions. There can be no assurance that other financial institutions or credit card issuers outside the United States will not enact additional restrictions. The loss of a major payment option would have a material adverse effect on our business, revenues, operating results and financial condition.

***There can be no assurance that the systems and protective measures we have in place will or can guarantee protection against fraudulent activities and unauthorized access from minors.***

There can be no assurance that the systems and protective measures we have in place will or can guarantee protection against fraudulent activities and unauthorized access from minors, which could have a material adverse effect on our reputation, business, revenue, operating results and financial conditions. We attempt to mitigate these concerns with systematic controls and a dedicated fraud team.

***In addition to regulations pertaining specifically to online gaming, we may become subject to any number of laws and regulations that may be adopted with respect to the Internet and electronic commerce.***

In addition to regulations pertaining specifically to online gaming, we may become subject to any number of laws and regulations that may be adopted with respect to the Internet and electronic commerce. New laws and regulations that address issues such as user privacy, pricing, online content regulation, taxation, advertising, intellectual property, information security, and the characteristics and quality of online products and services may be enacted. As well, current laws, which predate or are incompatible with the Internet and electronic commerce, may be applied and enforced in a manner that restricts the electronic commerce market. The application of such pre-existing laws regulating communications or commerce in the context of the Internet and electronic commerce is uncertain. Moreover, it may take years to determine the extent to which existing laws relating to issues such as intellectual property ownership and infringement, libel and personal privacy are applicable to the Internet.

The adoption of new laws or regulations relating to the Internet, or particular applications or interpretations of existing laws, could decrease the growth in the use of the Internet, decrease the demand for our products and services, increase our cost of doing business or could otherwise have a material adverse affect on our business, revenues, operating results and financial condition.

***Current global financial conditions have been characterized by increased volatility and several financial institutions have either gone into bankruptcy or have had to be rescued by governmental authorities. Access to public financing has been negatively impacted by both the rapid decline in value of sub-prime mortgages and the liquidity crisis affecting the asset-backed commercial paper market.***

Current global financial conditions have been characterized by increased volatility and several financial institutions have either gone into bankruptcy or have had to be assisted by governmental authorities. Access to public financing has been negatively impacted by both the rapid decline in value of sub-prime mortgages and the liquidity crisis affecting the asset-backed commercial paper market. As a result, several major economies have been in prolonged recessions, including but not limited to, the United Kingdom and Germany. If these economies do not recover in a timely manner, future revenues may be adversely impacted. Secondly, the disruption to the global finance markets may impact the ability of the Company to obtain equity or debt financing in the future on terms favorable to the Company. If such increased levels of volatility and market turmoil continue, the Company's operations could be adversely impacted and the trading price of the Common Shares may be adversely affected.

***There can be no assurance that the Internet infrastructure or the Company's own network systems will continue to be able to support the demands placed on it by the continued growth of the Internet, the overall online gaming industry or of our customers.***

The growth of Internet usage has caused frequent interruptions and delays in processing and transmitting data over the Internet. There can be no assurance that the Internet infrastructure or the Company's own network systems will continue to be able to support the demands placed on it by the continued growth of the Internet, the overall online gaming industry or of our customers.

The Internet's viability could be affected if the necessary infrastructure is not sufficient, or if other technologies and technological devices eclipse the Internet as a viable channel.

End-users of our software depend on Internet Service Providers (ISPs), online service providers and our system infrastructure for access to the Internet gaming sites operated by our licensees. Many of these services have experienced service outages in the past and could experience service outages, delays and other difficulties due to system failures, stability or interruption. Our licensees may lose customers as a result of delays or interruption in service, including delays or interruptions relating to high volumes of traffic or technological problems. As a result, we may not be able to meet service levels that we have contracted for, putting us in breach of contractual commitments, which in turn could materially adversely affect our business, revenues, operating results and financial condition.

***The demand and acceptance for new products and services are subject to a level of uncertainty and growing competition.***

The Internet gaming industry continues to evolve rapidly. The demand and acceptance for new products and services are subject to a level of uncertainty and growing competition, and if our services do not continue to receive market acceptance, our business, revenues, operating results and financial condition could be materially adversely affected.

***Our Internet gaming software and electronic commerce services are reliant on technologies and network systems to securely handle transactions and user information over the Internet, which may be vulnerable to system intrusions, unauthorized access or manipulation.***

Our Internet gaming software and electronic commerce services are reliant on technologies and network systems to securely handle transactions and user information over the Internet, which may be vulnerable to system intrusions, unauthorized access or manipulation. As users become increasingly sophisticated and devise new ways to commit fraud, our security and network systems may be tested and subject to attack. We have experienced such system attacks in the past and implemented measures to protect against these intrusions. However, there is no assurance that all such intrusions or attacks will or can be prevented in the future, and any system intrusion/attack may cause a delay, interruption or financial loss, which could have a material adverse effect on our business, revenue, operating results and financial condition.

***If ISPs experience service interruptions, communications over the Internet may be interrupted and impair our ability to carry on business***

Our electronic commerce product relies on ISPs to allow our licensees' customers and servers to communicate with each other. If ISPs experience service interruptions, the communications over Internet may be interrupted and impair our ability to carry on business. In addition, our ability to process e-commerce transactions depends on bank processing and credit card systems. In order to prepare for system problems, we are strengthening and enhancing our current facilities and the capability of our system infrastructure and support. Nevertheless, any system failure as a result of reliance on third parties, including network, software or hardware failure, which causes a delay or interruption in our e-commerce services could have a material adverse effect on our business, revenues, operating results and financial condition.

***Licensees of our software and services compete with existing and established recreational services and products, in addition to other forms of entertainment.***

Licensees of our software and services compete with existing and established recreational services and products, in addition to other forms of entertainment. Our success will depend, in part, upon our ability to keep pace with technological developments, respond to evolving customer requirements and achieve continued market acceptance.

We compete with a number of public and private companies, which provide electronic commerce and/or Internet gaming software. In addition to known current competitors, traditional land-based casino operators and other entities, many of which have significant financial resources, an entrenched position in markets and name-brand recognition, may provide Internet gaming services in the future, and thus become our competitors. As well, such companies may be able to require that their own software, rather than the software of others, including our gaming software or our e-cash systems and support, be used in connection with their payment mechanisms.

The barriers to entry into most Internet markets are relatively low, making them accessible to a large number of entities and individuals. We believe the principal competitive factors in our industry that create certain barriers to entry include reputation, technology, financial stability and resources, proven track record of successful operations, critical mass (particularly relating to online poker), regulatory compliance, independent oversight and transparency of business practices. While these barriers will limit those able to enter or compete effectively in the market, it is likely that new competitors will enter the market in the future.

Increased competition from current and future competitors has and may in the future result in price reductions and reduced margins, or may result in the loss of our market share, any of which could materially adversely affect our business, revenues, operating results and financial condition.

***In fiscal 2009, our top 7 licensees accounted for approximately 82% (2008: 81%) of our total revenue. In addition, all our key licensees operate from a limited number of licensing jurisdictions.***

In fiscal 2009, our top 7 licensees accounted for approximately 82% (2008: 81%) of our total revenue. In addition, all our key licensees operate from a limited number of licensing jurisdictions. The loss of one or more of these key licensees, or the loss of their license to operate in the limited number of licensing jurisdictions, could have a material adverse effect on our business, revenues, operating results and financial condition.

***Contracts are subject to renewal, renegotiation and may be contingent on certain performance requirements. There can be no assurance that license agreements will be renewed or that there will not be a material change in the terms of the contracts, which could adversely affect our business, revenues, operating results and financial condition.***

Licensing contracts generally have multi-year terms, are exclusive, and have renewal provisions, which provide us with a long term ongoing revenue stream. Contracts are subject to renewal, renegotiation and may be contingent on certain performance requirements. There can be no assurance that license agreements will be renewed or that there will not be a material change in the terms of the contracts, which could adversely affect our business, revenues, operating results and financial condition.

Similar issues exist in respect of brand licensing agreements. Our branded games business is dependant on our ability to continue to incorporate into our premium branded games, the intellectual property licensed to us by brand licensors, such as Marvel Comics, DC Comics, a division of Warner Bros., and Paramount Digital Entertainment. There can be no assurance that key brand license agreements will be renewed or that there will not be a material change in the terms of the contracts, which could adversely affect our business, revenues, operating results and financial condition.

***We are subject to exposure in regard to chargebacks, which may also result in possible penalties and elimination of payment options.***

We are subject to exposure in regard to chargebacks, which may also result in possible penalties and elimination of payment options. Chargebacks refer to any deposit transaction credited to a user's account that is later reversed or repudiated. While the Company has various control measures which seek to minimize exposure to chargebacks, it is not possible to entirely eliminate or prevent chargebacks, and a material increased incidence of chargebacks could have a material adverse effect on our business, revenues, operating results and financial conditions.

***There are certain difficulties and risks inherent in doing business internationally, including the burden of complying with multiple and conflicting regulatory requirements, foreign exchange controls, potential restrictions or tariffs on gaming activities that may be imposed.***

There are certain difficulties and risks inherent in doing business internationally, including the burden of complying with multiple and conflicting regulatory requirements, foreign exchange controls, potential restrictions or tariffs on gaming activities that may be imposed, potentially adverse tax consequences and tax risks, and changes in the political and economic stability, regulatory and taxation structures, and the interpretation thereof, of jurisdictions in which we, our subsidiaries and our licensees operate, and in which our licensees' customers are located, all of which could have a material adverse effect on our business, revenues, operating results and financial condition.

There can be no assurance that we will be able to sustain or increase revenue derived from international operations or that we will be able to penetrate linguistic, cultural or other barriers to new foreign markets.

***Fluctuations in the exchange rate of world currencies could have a positive or negative effect on our reported results.***

Our financial results are reported in U.S. currency, which is subject to fluctuations as against the value of the currencies of the countries in which we operate, including British pounds, euro, and Canadian dollars. Fluctuations in the exchange rate of world currencies could have a positive or negative effect on our reported results. We may utilize a hedging program from time to time and/or take advantage of the natural hedge in having operations in multiple currencies to mitigate a portion of our currency risks, but there can be no assurance that we will not experience currency losses in the future, which could have a material adverse effect on our business, revenues, operating results and financial condition.

***Our effective tax rate in the future could be adversely affected by changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities and changes in tax laws.***

We are subject to income taxes in Ireland, Canada, Cyprus, Malta and other jurisdictions. Our tax calculations involve estimations in several areas including, but not limited to, transfer pricing. Tax authorities may disagree with our estimations and assess additional taxes. We regularly review the likely outcomes of such assessments in order to determine the appropriateness of our tax provision. However, actual outcomes may differ and could have a material impact on our net income or financial condition. In addition, our effective tax rate in the future could be adversely affected by changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities and changes in tax laws. In particular, the carrying value of future tax assets is dependent on our ability to generate future taxable income in the jurisdiction where we have recognized the deferred tax assets.

***We may be involved in litigation arising in the ordinary course and conduct of business. The outcome of such matters cannot be predicted with certainty, and could have a material adverse effect on our business, revenues, operating results and financial condition.***

We may be involved in litigation arising in the ordinary course and conduct of business. The outcome of such matters cannot be predicted with certainty, and could have a material adverse effect on our business, revenues, operating results and financial condition.

Moreover, from time to time, third parties have asserted and may continue to assert patent, trademark, copyright and other intellectual property rights to technologies or business methods that we consider important. There can be no assurance that the assertion of such claims will not result in litigation or that we would prevail in any such litigation or be able to obtain a license for the use of any infringed intellectual property from a third party or, if such a license is required, that it would be available on terms acceptable to us.

On March 30, 2010, the Company delivered to Marvel a Statement of Claim regarding an alleged breach by Marvel of certain provisions of its agreement with the Company relating to the licensing of Marvel comic book characters to CryptoLogic. Any proceeding flowing from the said Statement of Claim must proceed by way of arbitration in the City of New York and under New York law, as per the contract with Marvel.

***Our competitive position is dependent in part upon our ability to protect our proprietary technology.***

We rely on a combination of laws and contractual provisions to establish and protect our rights in our software and proprietary technology. We believe that our competitive position is dependent in part upon our ability to protect our proprietary technology. We generally enter into non-disclosure and invention agreements with employees, licensees, consultants and customers, and historically have restricted access to our software products source codes. We regard our source code as proprietary information, and attempt to protect the source code versions of our products as trade secrets and unpublished copyrighted works. Despite our precautions and measures implemented to protect against such attempts, unauthorized parties may have or could in the future copy or otherwise reverse engineer portions of our products or otherwise obtain and use information that we regard as proprietary.

Our Company has patents and trademarks in certain jurisdictions and is in the process of applying for further trademark registrations and patents, which may provide such protection in relevant jurisdictions. However, there can be no assurance that this will be sufficient to fully protect our proprietary technology. In addition, certain provisions of our license agreements, including provisions protecting against unauthorized use, transfer and disclosure, may be found to be unenforceable in certain jurisdictions.

We believe that patent, trademark, copyright and other legal protections are less significant to our success than other factors such as the knowledge, ability and experience of our personnel, new product and service developments, frequent product enhancements, customer service and ongoing product support.

We also have a proprietary interest in our name. The names CryptoLogic and WagerLogic have become known in the Internet gaming industry. Accordingly, our competitive position could be affected if our name was misappropriated and our reputation in any way compromised.

There can be no assurance that the steps we have taken to protect our proprietary rights will be adequate to deter misappropriation of our technology or independent development by others of technologies that are substantially equivalent or superior to our technology. Any misappropriation of our name, technology or development of competitive technologies could have a material adverse effect on our business, revenues, operating results and financial condition.

Due to the complex, sophisticated and global nature of the business, there can be no assurance that there has been no breach of third parties intellectual property rights by the Company, and any adverse judgment in this regard could have a material adverse effect on our business, revenues, operating results and financial condition.

***Our future success is dependent on certain key management and technical personnel.***

Our future success is dependent on certain key management and technical personnel. The loss of these individuals or the inability to attract and retain highly qualified employees and advisors could have a material adverse effect on our business, revenues, operating results and financial condition.

***The expansion of our business and the increasing complexity of our product offerings, coupled with the rapid evolution of our markets, are expected to continue to place a significant strain on our management and operational resources and to increase demands on our internal systems, procedures and controls.***

The expansion of our business and the increasing complexity of our product offerings, coupled with the rapid evolution of our markets, are expected to continue to place a significant strain on our management and operational resources and to increase demands on our internal systems, procedures and controls. Our future operating results will depend on management's ability to develop and manage growth, enhance our products and services to respond to market demand, deal with competition and evolving customer requirements, manage our system infrastructure and requirements to meet the growing demands of our business, hire and retain significant numbers of qualified employees, accurately forecast revenues and control expenses. A decline in our revenues without a corresponding and timely slowdown in our expenses, or our inability to manage or build future growth efficiently, could have a material adverse effect on our business, revenues, operating results and financial condition.

***The market price of our common shares has experienced significant fluctuation and may continue to fluctuate significantly.***

The market price of our common shares has experienced significant fluctuation and may continue to fluctuate significantly. The market price of our common shares may be adversely affected by various factors, such as proposed Internet gaming legislation or enforcement of existing laws, the loss of a customer, the announcement of new products or enhancements, innovation and technological changes, quarterly variations in revenue and results of operations, changes in earnings estimates by financial analysts, speculation in the press or analyst community and general market conditions or market conditions specific to particular industries, including the Internet and gaming.

In addition, the stock market has from time to time experienced extreme price and volume fluctuations. These company-specific or broad market fluctuations may adversely affect the market price for our common shares. Anti-online gaming legislation could also impact our ability to remain listed.

Although our common shares are listed and traded on the Toronto Stock Exchange, the NASDAQ Global Select Market and the London Stock Exchange's Main Market, this should not imply that there will always be a liquid market in our Common Shares. In addition, pursuant to a business reorganization completed in 2007 (see page 1) exchangeable shares of an indirect subsidiary of the Company, CEC were issued, and are listed and traded on the Toronto Stock Exchange. Because of separate listings, the trading prices of the Common Shares and CEC shares may not reflect equivalent values. Company-specific or broader market fluctuations may adversely affect the market price of the exchangeable shares, and there can be no assurance that there will continue to be an active market for these securities.

***We may incur losses and further declines in revenue in future periods.***

We have incurred losses in recent periods. We recorded a net loss of \$35.5 million for the year ended December 31, 2009, and a net loss of \$32.7 million for the year ended December 31, 2008. We may incur losses and further declines in revenue in the future periods. If we incur additional losses and our cash resources and financing options are insufficient, our ability to operate would be adversely impacted.

**ITEM 4. INFORMATION ON THE COMPANY**

**A. HISTORY AND DEVELOPMENT OF THE COMPANY**

The Company originally was formed by articles of amalgamation under the *Business Corporations Act* (Ontario) effective March 7, 1996 pursuant to an amalgamation agreement dated January 19, 1996 between Inter.tain.net Inc., a private corporation, and Biroco Kirkland Mines Limited. Immediately prior to the amalgamation, Biroco Kirkland Mines Limited did not carry on active operations. On June 28, 1996, we changed our name from Inter.tain.net Inc. to CryptoLogic Inc. Currently, the Company operates under CryptoLogic Limited.

On June 1, 2007, in order to advance its global strategy, the Company moved its headquarters from Canada to the Republic of Ireland by forming a new parent company, CryptoLogic Limited, a company incorporated under the laws of Guernsey with its place of business in Dublin, Ireland. This business reorganization was implemented by way of an Ontario, Canada Superior Court of Justice court approved plan of arrangement (the Arrangement) and approved by the shareholders on May 24, 2007. CryptoLogic Limited acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., which through the Arrangement, became an indirect subsidiary of CryptoLogic Limited.

Our registered office is located at 1 Le Marchant Street, St. Peter Port, Guernsey, Channel Islands, GY1 4HP. Our head office is located at Marine House, Clanwilliam Place, Dublin 2, Ireland, and its telephone number is 353-(0)1-234-0400.

Our head office provides executive functions to our corporate group. Our subsidiary, WagerLogic, through its offices in Cyprus, Malta and the U.K., provides software, licensing, e-cash systems and support, customer support and marketing support services for our Internet gaming software to third-party gaming operators. Our Toronto, Canada office provides software development, upgrades and technical support for WagerLogic as well as all usual administrative functions.

**B. BUSINESS OVERVIEW**

We are a pioneer and a global leading software developer and services provider to the global Internet gaming market (excluding the U.S.). We are one of the industry's longest-established publicly traded online gaming software companies.

Through our WagerLogic subsidiaries in Cyprus, Malta and the U.K., we provide software hosting and licensing, e-cash systems and support, customer support and marketing support services for our Internet gaming software to third-party gaming operators. We also offer access to a highly liquid poker room operated by GTECH, a third party. WagerLogic licenses our software products and provides services to an international client base (licensees or customers), while retaining ownership and control of the software. Our software offers a complete online gaming solution to our licensees, comprising:

A broad, turn-key Internet-based game suite providing a casino and access to a highly liquid poker room. Our game suite features:

- o more than 346 download and non-download casino table and slot games;
- o multi-languages (English, Spanish, Greek, Japanese, Chinese, French, German, Italian);
- o multi-currencies (U.S. dollars, British pounds and euro); and
- o multi-platforms (download, non-download (Java and Flash), wireless);

E-cash systems and support for player deposits and withdrawals;

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Business intelligence and data analysis tools to assist licensees in their marketing efforts;

Licensee support through WagerLogic's extended hour, multi-language customer support; and

Marketing support services, to assist licensees in developing and executing strategies for marketing their online gaming businesses.

2009 was an extremely difficult year for Cryptologic as the Company implemented its new strategy aimed at returning the Company to profitability and long-term growth against the backdrop of a severe global economic downturn, a slower than anticipated seasonal up-tick in fourth quarter revenue and unanticipated licensee-delays in the roll-out of branded games.

The new strategy, however, continues a tradition that the Company has of being a pioneer in the global Internet gaming market. Founded in 1995, we launched the world's first on-line casino games that year. With a resilient and scalable platform, a commitment to developing the best games in the marketplace and complemented with excellent customer support, the Company thereafter secured an excellent reputation for its product offering. However, changing market conditions in 2006 and 2007 meant that the model was no longer viable and had to change.

During 2008 the management team announced a new business strategy for the Company, and in 2009 we focused on the transition towards that goal. In essence, the new business model is centered on the Company evolving from being purely a developer and licensor of poker and casino software on its own network, to one which still develops and licenses an excellent casino product, but also delivers high-quality, branded and non-branded games to the industry at large. This effectively opens up a new market and revenue stream for the Company. It also allows us to make our former competitors collaborative partners in our growth. It is a good example of the "build once, license often" model that has been and continues to be successful in the software industry.

Also, in order to effect this transition and plan for sustainable growth, it was critical that the Company distill its knowledge and understanding of games, the gaming industry and evolving technologies into a single environment, resulting in the creation of the Cryptologic Center for Innovation. This is a virtual group of people and partners committed to delivering innovative new products to our licensees and will act as a springboard for all of our future development activities.

Notwithstanding the foregoing, 2009 was distinguished around the world for generally poor and uncertain trading conditions and Cryptologic was not immune. This is reflected in our lower revenue as compared to 2008. Nevertheless, good progress was made on a number of fronts, including a significant number of new licensee signings; the creation of a healthy pipeline of future new business; more effective use of our Remote Development Centers; a simplification of our technology infrastructure, and a reduction in workforce and cost base.

Launching a new strategy in the midst of extremely challenging global macro-economic conditions tests the merits of any company's business model. We believe that ours has begun to prove itself capable of supporting long-term growth. Management is determined to focus on the development and support of the hosted casino business while continuing to build on the success of our branded games initiative by expanding our partnerships and broadening the types of games we offer. At the same time, we intend to maintain our downward pressure on our recurring cost base (down \$20.6 million in 2009) which has produced a leaner, smarter, more flexible business, that is capable not only of responding to changing market demands but, in some cases, leading them.

Cryptologic's strategy has three main elements:

Focusing on our core Internet hosted casino business. For five consecutive years, readers of *Gambling Online* magazine have voted our casino games the best in the industry. These award-winning games are complemented by a widely acclaimed support services structure. We intend to capitalize on this success by continuing to invest in new casino games which will further expand our respected portfolio.

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Licensing our best branded games to others, creating an attractive new revenue stream and turning former competitors into collaborators. The philosophy is simple: build once, license often. Through working with highly respected content providers and brand owners we have successfully delivered the likes of Spiderman, The Hulk and Batman to both our own hosted casino licensees and to the market in general, thus receiving a greater return from our investment dollar. Concentrating on being a leading innovator. By that we mean, not just developing and deploying new ideas, but new ideas that force the market to think and react.

For this strategy to be successful, it demands the establishment of an expanding network of licensees and channel partners, and once established, the strengthening, and deepening of those relationships. Cryptologic has forged excellent relationships with many licensees including two of the largest and most successful in the industry: 888.com and Party Gaming both of whom are deriving significant revenue and benefits from licensing a sample range of our products.

Our flexible business model and the quality of our offering allowed 2009 to be the most successful year in Cryptologic's history in terms of customer acquisition. Among the new signings and launches are such well known brands as:

Sky  
Betfair  
Unibet  
Gala Coral  
Virgin  
Bet24  
The Tote  
Sportingbet  
Victor Chandler

Additional product launches were achieved through our new brand licensing agreements with companies such as DC Comics, a division of Warner Bros, and Paramount as well as ongoing releases using brands licensed from the long-standing partners like CapCom and Marvel.

We believe these partnerships offer the potential for significant future growth based upon both the brand recognition and loyalty associated with these partners and their unique and distinctive intellectual property. This, however, is not enough. It is vital that a company the size of Cryptologic compete in a most effective manner and that means, to us, leading in innovation – namely, the ability to deliver offerings to the market that cause people to stop and take notice. Our goal is to set ourselves apart from our larger competitors, and also possible new entrants, by creating offerings that are both new and innovative. The goal is simple – create offerings and business models that cause others to play catch-up. Cryptologic's ability to reduce the development and deployment time for a game by 75% is a case in point. Further offerings in 2010 will serve as additional proof points.

MARKETING OPPORTUNITY

We currently market our technology and services through a select sales and marketing strategy whereby we identify key potential customers that meet our licensee profile, and then contact such prospects directly. We also attend industry trade shows around the world to generate new prospects, and respond to referrals from existing customers and other industry participants. CryptoLogic has generally sought licensees with an established brand, an audience with a propensity to gamble, and sufficient resources and commitment to successfully market the business.

In Internet casino, the key to success is differentiation through the combination of our new and innovative games, a robust e-wallet with multiple payment options and effective marketing to players by our licensees. CryptoLogic will continue to pursue new casino opportunities emphasizing brand name licensees with marketing commitment. In branded games, the key to success is the strategic partnerships established by CryptoLogic with trusted media brands such as Marvel Comics, DC Comics, a division of Warner Bros, and Paramount Digital Entertainment.

REVENUE SOURCES

Substantially all of our revenue is of a recurring nature in that WagerLogic's licensees pay an ongoing fee each month over the contract term for the licensing and support of our software or branded games, calculated as a percentage of each licensee's level of activity. Additional revenues are derived from other sources including fees for the provision of software customization, and advertising and marketing services related to our portal business. Historically, we experience seasonality with slower sales in the second and third quarters, as the use of the Internet is not as strong in the summer months when players tend to spend less time indoors and at their computers. The global e-gaming industry experienced a downturn in 2009 and continues to face challenges early in 2010.

In 2009, revenue was \$39.8 million (2008: \$61.5 million, 2007: \$73.7 million), with 91.2% (2008: 90.9%, 2007: 93.6%) of this amount represented by ongoing software licensing fees or royalties. Other revenue sources, which primarily included fees for software customization and advertising and marketing services generated from our portal business, accounted for 8.8% of total revenue (2008: 9.1%, 2007: 6.4%).

Fee revenue from our Internet casino business and branded game business is calculated as a percentage of a licensee's level of activity in its online casino site. By contrast, fees from Internet poker are based on a percentage of the licensee's rake per hand in regular or ring games (the rake is typically 5% of the pot, up to a maximum amount per hand), or fixed fees for entry into poker tournaments. \$30.0 million or 75.3% of our total revenue was derived from our casino business in 2009 (2008: \$41.8 million or 68.0%, 2007: \$49.5 million or 67.1%). Branded games revenue was \$2.8 million or 7.1% of our total revenue in 2009 (2008: \$0.3 million or 0.5%, 2007: NIL). Internet poker fees were \$3.5 million or 8.8% of total revenue in 2009 (2008: \$13.8 million or 22.4%, 2007: \$19.5 million or 26.5%).

As at December 31, 2009, we had 32 licensees located around the world, including well-known U.K. and global land-based gaming organizations, which operate under government authority where their Internet business subsidiaries are domiciled. Our top 7 licensees in 2009 accounted for approximately 82% of our total revenue (2008: 81%, 2007: 79%). All of our hosted casino licensees operate from one licensing jurisdiction serving customers based in multiple countries

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The Company's principal geographic markets are in the U.K. and Continental Europe:

<b>For the Years Ended December 31,</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
United Kingdom	48%	58%	49%
Europe	40%	33%	40%
United States	0%	0%	0%
Other	12%	9%	11%
<b>Total <sup>(1)</sup></b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

<sup>(1)</sup> The Company does not have revenue data by geographic market for its branded game licensees. Branded game revenue was 7.1% of revenue in 2009 and 0.5% of revenue in 2008 (2007: nil).

### PRODUCTS AND SERVICES

Our Internet-based gaming and electronic commerce software products (i.e. hosted casino) are used by licensees to create virtual casinos. The downloadable software package transfers the front-end information (i.e., playing cards, roulette wheel, dice numbers) between users and remote servers. The software package utilizes each user's computer to generate the graphics of the virtual gaming site, while the gaming servers perform the dealer function, generating the random numbers of playing cards, roulette numbers and dice numbers, as applicable. Many of our most popular casino games are also available on either the Flash or Java platforms, which provide an entertaining gaming experience without having to wait for software to download.

Among other things, our software contains proprietary encryption features, which allows secure transmission of data, and permits our licensees to offer multi-player games, a panoramic virtual casino floor populated by real players, progressive jackpots, Internet browsing features and inter-player chatting.

As part of our commitment to safe and responsible gaming, our gaming solution provides personal options and security features including deposit and bet limits, temporary and permanent account locks, personal identification verification, and online tracking of a player's gaming activity and financial transactions. We are also able to restrict registration and game play from residents of prohibited jurisdictions.

Our gaming solution is complemented by e-cash systems and support. We provide Internet-based electronic commerce support and technology to our licensees and their respective customers and maintain, through subsidiaries, electronic commerce accounts for both merchants of our electronic commerce software and their end-users.

For the majority of our licensees, we report and remit to them the net transaction revenues less licensing and support fees payable to the Company (as specified in the applicable licensing agreements). Some licensees have responsibility for their own e-cash systems and support to enable an integrated single player account for all their online offerings, and in such cases, the licensees report and remit licensing fees to us.

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Using our e-cash software, players can use a wide range of payment options, including credit and debit card and various electronic wallets. Web cashier accounts can be opened in United States dollars, British pounds, and euro.

To assist our licensees in retaining players and re-activating lapsed accounts, we have invested significantly in our customer relationship management solution. We have introduced and improved our back-office offering with sophisticated business intelligence, data warehousing and marketing tools to assist licensees in understanding, servicing and building one-on-one relationships with their players.

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We also provide extended hour, multi language customer support in the languages and currencies supported by our software for enhanced convenience to our licensees' global player base. Our customer support is available to help players with technical questions or assist with the gaming software and e-cash accounts.

We view our marketing support services as a key differentiator in our product and service offerings, as they form a key part of the Company's brand ownership and management strategy. For example, OIGE CG Limited, operator of the InterCasino brand, uses our marketing support services.

It is our objective to continue to introduce innovative software products, support tools and services that appeal to broad segments of gaming audiences worldwide. Since 2008, the Company has introduced 38 slot and casino table games and brought many well known entertainment brands to the Internet casino space. Highlights include unique, first-to-market offerings such as:

The Internet's first and only multi-currency jackpot video slot games featuring popular Marvel action characters such as *The Incredible Hulk*, *Daredevil*, *X-Men*, *Thor*, *Elektra*, *Ghost Rider*, *Spider-Man* and *The Fantastic Four*, and, more recently, *Sub Mariner*. All these brands have been exclusively licensed for CryptoLogic-developed games;

The world's first and only play-for-real slot versions of highly popular online casual games, such as *Cubis*, an award-winning, three-dimensional puzzle game, and *Bejeweled*, a gem-matching game – both among the most played games on AOL, MSN and other major portals – and most recently *Jewel Quest*, a popular puzzle-match game;

Our own patented games including the progressive jackpot slot, *Millionaires Club*, which awarded the two largest online jackpots in history; and a new patent-pending game, *Multi-Hand Video Blackjack*, which brings together blackjack and video poker;

Our own *Texas Hold'em Bonus Poker*, which is the first-ever online version of the widely popular land-based casino game and combines the huge popularity of poker with the excitement of a casino card game; and

The Internet's first Fruit Machines, a tradition in U.K. pubs.

The first-ever slot version of the world-famous *Street Fighter II* arcade game.

New games, introduced in 2009, based on world-famous DC Comics characters such as *Superman*, *Batman*, *Wonder Woman* and others.

Having established exclusive relationships with major media companies such as Marvel Comics, DC Comics, a division of Warner Bros., and Paramount Digital Entertainment, we have created industry leading casino games, which are a key component of our hosted casino product. Through our branded games business, we are able to offer these games not only to our hosted casino customers, but to the entire industry at large.

We also operate a gaming portal business under two brands: Casino.co.uk and WinnerOnLine. These portals earn advertising revenue from gaming operators, and direct traffic to operator sites and those sites owned by the Company's licensees – providing a known-name marketing channel and a player acquisition tool for licensees.

PATENTS AND OTHER INTELLECTUAL PROPERTY

Our general policy has been to seek patent protection for gaming innovations where proprietary rights will improve our competitive position. We hold a series of patents including one related to our *Millionaires Club* slot game, which offers million-dollar-plus online jackpots, and one related to our Multi-Hand Video Blackjack game. We also have patents pending on various other gaming innovations.

We also license intellectual property, generally on an exclusive basis, from third parties for use in our games including the world's first and only play-for-real, slot version of the popular gem-matching game, *Bejeweled*, and the Internet's first and only multi-currency jackpot video slot games featuring popular DC Comics action characters such as *Superman* and *Wonder Woman*.

*See Item 3.Key Information Risk Factors*

GLOBAL REGULATORY ENVIRONMENT

While the United Kingdom and other European jurisdictions such as Malta have currently adopted a regime which permits its licensees to accept wagers from any jurisdiction differing approaches are developing in other parts of Europe. Some European countries, including Italy and France, have, or are in the process of implementing regimes which only permit the targeting of the domestic market provided a local license is obtained and local taxes accounted for. Other European territories continue to defend a licensing regime that limits supplies of gambling to a local monopoly and have combined this with an attempt to outlaw all other supplies. Either of these restrictive approaches may yet be deemed to be in potential conflict (in any specific jurisdiction) with EU treaty law (governing the free movement of goods and services throughout the European Union) and case law rendered by the European Court of Justice ( ECJ ). However, although judgments of the ECJ had been critical of anti gambling laws in certain territories there have recently been several decisions and Advocate General opinions published which suggest that the restrictive approach adopted in some countries is now considered to be defensible. Nonetheless, the actions of the European Commission ( EC ) has looked at creating directives that could harmonize the treatment and operation of online gaming throughout the EU, which would be in line with the EC's goal of encouraging a free and open market throughout the entire union. There is no indication that any such directive will ever be introduced however, as there remains a great deal of political opposition. Moreover, the EC has also initiated infringement proceedings against some EU member states in relation to alleged breaches of Article 56 of the Treaty on the Functionality of the European Union, which article enshrines the principle of freedom of movement of services, but in most cases these have not reached conclusion.

Since 1995, online gaming has grown into a large, multi-billion dollar industry, but with regulatory inconsistencies among countries and limited formal regulation. Laws around the world are often outdated, ambiguous and continue to develop on a country-by-country basis.

On October 13, 2006, the U.S. enacted the UIGEA, which effectively banned online gaming in that country by making it illegal to process related financial transactions. The industry-wide impact of UIGEA has negatively affected our business by significantly reducing our revenue and earnings..

At the time the UIGEA was enacted, the entire U.S. market was estimated to represent approximately 50% of the global online gaming market (source: GBGC). However, the online casino and online poker markets outside the U.S., the core areas of our business, are expected to continue to grow. Prior to the enactment of UIGEA, approximately 70% of our licensees' revenue was derived from non-U.S. sources due to our global diversification strategy. Since 2002, we have focused on licensees that primarily target non-U.S. markets, most notably the U.K. and Continental Europe. After the UIGEA enactment, 100% of licensees' revenue came from outside the U.S.



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In September 2007, the UK Gaming Act came into force, which Act regulates online gaming in that jurisdiction, and is generally viewed as a positive development for the industry, our customers and for CryptoLogic. Most of the underlying rules and codes in relation to entities established in the UK, or marketing into the UK, have now been enacted. However, there is no assurance that the UK regulatory regime as interpreted by the Gambling Commission, the Gambling Act's independent regulator, will provide a commercially-viable market and may create restrictions that will have a material adverse effect on our customers, our business, revenues, operating results and financial condition. Indeed, the DCMS (the government body with responsibility for overseeing gambling), has recently announced that it may reconsider one of the main tenets of the Gambling Act, namely that if an online gaming operator was regulated either in Europe or in a jurisdiction approved by the DCMS (the so called "white listed" jurisdictions) such an operator could fully target the UK gambling market. It seems likely that instead that the DCMS will recommend (in a report to be published imminently) that it will require entities not licensed in the UK to acquire some form of additional accreditation to access the UK market and/or pay taxes in the UK.

Elsewhere in Europe the legislative environment continues to evolve, with some countries showing signs of following the U.K.'s lead to implement a licensing regime while others continue to protect state gambling monopolies. As emphasized, the EC has commenced infringement proceedings against various member states that are taking a protectionist approach—a development that we believe is favorable to the industry in Europe. While most decisions rendered by the ECJ over the past several years have been broadly favorable to the industry, it nonetheless upheld the Portuguese monopoly in the La Liga case and more recently there have been several Advocate General opinions published which would suggest that certain jurisdictions' protectionist approach is not going to be found by the ECJ to be contrary to EC treaty law (the court normally follows the Advocate General's views in the judgments given usually several months after the publication of the opinion).

CryptoLogic has long advocated a regulatory approach to foster a transparent, credible and growing online gaming industry. We believe that government plays an important role and is in the best position to regulate this industry to provide consumer protection, preserve the integrity of the online gaming industry, and build a credible and business-friendly marketplace. We have sought and achieved certification of our software in strictly regulated jurisdictions. It is through this process that we maintain our reputation as the pioneer in online gaming and a trusted provider for licensees and their customers.

For more information regarding the global regulatory environment in which the Company and its licensees do business, refer to "Risks Related to the Industry" under "Item 3. Key Information."

### COMPETITIVE ENVIRONMENT

We compete with a number of public and private companies, which provide electronic commerce and/or Internet gaming software. Given the stage of development of the industry and the number of private organizations operating in the industry, information about the nature of our competitors, their operations and their resources is difficult to compile. In addition to current known competitors, traditional land-based gaming operators and other entities, many of which have significant financial resources and name-brand recognition, may provide Internet gaming services in the future, and thus become our competitors. Increased competition from current and future competitors and increased expenditures has and could continue to result in the reduction of our margins, or could result in the loss of our market share.

Licensees of our software and branded games compete with existing and more established recreational services and products, in addition to other forms of entertainment. Our success will depend, in part, upon our ability to enhance our products and services, expand our system infrastructure and resiliency, keep pace with technological developments, respond to evolving customer requirements and achieve continued market acceptance.

While it is difficult to confirm the exact number of Internet gaming sites since most companies are private, GBGC estimates there are around 2,400 online gaming properties down from more than 2,800 several years ago. This decrease points to industry consolidation. As Internet gaming has developed and increased in sophistication,



so have the players who can choose from a proliferation of sites. Competition for players' attention and share of wallet is intensifying, and players are demanding more value, more games and an enhanced entertainment experience.

The global nature of the Internet makes most Internet markets, including the online gaming industry, relatively accessible to a wide number of entities and individuals. We believe the principal competitive factors in our industry that create certain barriers to entry include reputation, technology, financial stability and resources, proven track record of successful operations, critical mass, regulatory compliance, independent oversight and transparency of business practices. While these barriers will limit those able to enter or compete effectively in the market, it is likely that new competitors will be established in the future, in addition to known current competitors.

The bulk of CryptoLogic's revenue is generated through gaming activity in Europe. Many parts of Europe continue to experience a deep recession, which has negatively impacted the company's revenues. Revenue recovery for the company will in part depend on a broader recovery of economic conditions in key European markets.

### **C. ORGANIZATIONAL STRUCTURE**

The organizational structure of the Company as of December 31, 2009 is set forth below. CryptoLogic Limited, a company incorporated under the laws of Guernsey with its corporate headquarters in Dublin, Ireland, provides executive functions to our corporate group. Our subsidiary CryptoLogic Inc. is located in Canada, and provides software development, upgrades and technical support for our WagerLogic Limited subsidiary. With offices in Cyprus, Malta and the U.K., the WagerLogic group of companies provides software, licensing for our Internet gaming software, e-cash systems and support, customer support, marketing support and other services to third-party gaming operators or licensees around the world. During 2010, the Company intends to move its operations currently performed in Cyprus to Malta. Our ECash Direct subsidiary provides e-cash systems and support that enables licensees' players to deposit and withdraw funds through a wide range of payment options for use with the licensee. Our AdsDotCom subsidiary offers marketing services to our hosted casino licensees. Our CryptoLogic Asia subsidiary is responsible for advancing the Company's strategy and business development in Asia.

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CryptoLogic Exchange Corporation and CryptoLogic Callco ULC exist solely to facilitate the exchange of shares for CryptoLogic Limited in connection with the Arrangement (refer to page 1 of this annual report for further information regarding the Arrangement).

### **D. PROPERTY, PLANTS AND EQUIPMENT**

The following table sets forth the Company's principal leased properties.

Company	Location	Principal Use	Approx. Area (sq. ft.)	Term of Lease	Current Rent (per annum or to completion of term)
CryptoLogic Limited	Dublin, Ireland	Head office	5,400	4 years 10 months	182,758
CryptoLogic Limited	Dublin, Ireland	Head office	1,440	3 years 6 months	47,995
CryptoLogic Inc.	Toronto, Canada	Research and development	40,834	7 months	C\$779,385
CryptoLogic Inc.	Toronto, Canada	Research and development	11,426	7 months	C\$218,084
WagerLogic Limited	Nicosia, Cyprus	Software licensing and support	5,080	6 months	26,715
Ads Dot Com Limited	London, England	Marketing support	4,880	3 years 5 months	£291,556
WagerLogic Malta Software Limited	Msida, Malta	Software licensing and support	12,917	10 years	96,000

In December 2009, in accordance with the rental agreement, the Company exercised its right to exit the leasehold premises in Toronto and recorded termination costs of \$1.8 million payable on termination in July 2010.

### **ITEM 4A. UNRESOLVED STAFF COMMENTS**

Not applicable.

### **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

The Company's consolidated financial statements have been prepared in accordance with Canadian GAAP. The significant measurement differences between Canadian GAAP and U.S. GAAP for the years ended December 31, 2009, 2008 and 2007 are disclosed in Note 21 to our audited consolidated financial statements for the years ended December 31, 2009, 2008 and 2007.

The following discussion should be read in conjunction with our consolidated financial statements and related notes for the years ended December 31, 2009, 2008 and 2007 as set out in this annual report under Item 17. Financial Statements.



## **OVERVIEW**

2009 was an extremely difficult year for Cryptologic as the Company implemented its new strategy aimed at returning the Company to profitability and long-term growth against the backdrop of a severe global economic downturn, a slower than anticipated seasonal up-tick in fourth quarter revenue and unanticipated licensee-delays in the roll-out of branded games.

The new strategy, however, continues a tradition that the Company has of being a pioneer in the global Internet gaming market. Founded in 1995, we launched the world's first on-line casino games that year. With a resilient and scalable platform, a commitment to developing the best games in the marketplace and complemented with excellent customer support, the Company thereafter secured an excellent reputation for its product offering. However, changing market conditions in 2006 and 2007 meant that the model was no longer viable and had to change.

During 2008 the management team announced a new business strategy for the Company, and in 2009 we focused on the transition towards that goal. In essence, the new business model is centered on the Company evolving from being purely a developer and licensor of poker and casino software on its own network, to one which still develops and licenses an excellent casino product, but also delivers high-quality, branded and non-branded games to the industry at large. This effectively opens up a new market and revenue stream for the Company. It also allows us to make our former competitors collaborative partners in our growth. It is a good example of the "build once, license often" model that has been and continues to be successful in the software industry.

Also, in order to effect this transition and plan for sustainable growth, it was critical that the Company distill its knowledge and understanding of games, the gaming industry and evolving technologies into a single environment, resulting in the creation of the Cryptologic Center for Innovation. This is a virtual group of people and partners committed to delivering innovative new products to our licensees and will act as a springboard for all of our future development activities.

Notwithstanding the foregoing, 2009 was distinguished around the world for generally poor and uncertain trading conditions and Cryptologic was not immune. This is reflected in our lower revenue as compared to 2008. Nevertheless, good progress was made on a number of fronts, including a significant number of new licensee signings; the creation of a healthy pipeline of future new business; more effective use of our Remote Development Centers; a simplification of our technology infrastructure, and a reduction in workforce and cost base.

## **A STRATEGY FOR SUSTAINABLE GROWTH**

Launching a new strategy in the midst of extremely challenging global macro-economic conditions tests the merits of any company's business model. We believe that ours has begun to prove itself capable of supporting long-term growth. Management is determined to focus on the development and support of the hosted casino business while continuing to build on the success of our branded games initiative by expanding our partnerships and broadening the types of games we offer. At the same time, we intend to maintain our downward pressure on our recurring cost base (down \$20.6 million in 2009) which has produced a leaner, smarter, more flexible business, that is capable not only of responding to changing market demands but, in some cases, leading them.

Cryptologic's strategy has three main elements:

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Focusing on our core Internet hosted casino business. For five consecutive years, readers of Gambling Online magazine have voted our casino games the best in the industry. These award-winning games are complemented by a widely acclaimed support services structure. We intend to capitalize on this success by continuing to invest in new casino games which will further expand our respected portfolio.

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Licensing our best branded games to others, creating an attractive new revenue stream and turning former competitors into collaborators. The philosophy is simple: build once, license often. Through working with highly respected content providers and brand owners we have successfully delivered the likes of Spiderman, The Hulk and Batman to both our own hosted casino licensees and to the market in general, thus receiving a greater return from our investment dollar. Concentrating on being a leading innovator. By that we mean, not just developing and deploying new ideas, but new ideas that force the market to think and react.

For this strategy to be successful, it demands the establishment of an expanding network of licensees and channel partners, and once established, the strengthening, and deepening of those relationships. Cryptologic has forged excellent relationships with many licensees including two of the largest and most successful in the industry: 888.com and Party Gaming both of whom are deriving significant revenue and benefits from licensing a sample range of our products.

Our flexible business model and the quality of our offering allowed 2009 to be the most successful year in Cryptologic's history in terms of customer acquisition. Among the new signings and launches are such well known brands as:

Sky

Betfair

Unibet

Gala Coral

Virgin

Bet24

The Tote

Sportingbet

Victor Chandler

Additional product launches were achieved through our new brand licensing agreements with companies such as DC Comics, a division of Warner Bros, and Paramount as well as ongoing releases using brands licensed from the long-standing partners like CapCom and Marvel.

We believe these partnerships offer the potential for significant future growth based upon both the brand recognition and loyalty associated with these partners and their unique and distinctive intellectual property. This, however, is not enough. It is vital that a company the size of Cryptologic compete in a most effective manner and that means, to us, leading in innovation – namely, the ability to deliver offerings to the market that cause people to stop and take notice. Our goal is to set ourselves apart from our larger competitors, and also possible new entrants, by creating offerings that are both new and innovative. The goal is simple – create offerings and business models that cause others to play catch-up. Cryptologic's ability to reduce the development and deployment time for a game by 75% is a case in point. Further offerings in 2010 will serve as additional proof points.

### **PRODUCT PERFORMANCE**

As a developer of software, one of Cryptologic's particular strengths is its ability to bring new products to the market quickly and cost effectively. This necessitates a very close working relationship with our brand and content suppliers (the likes of Paramount, DC Comics NextGen, etc.), our Remote Development Centers, our Innovation Center, our Business Development Group and, naturally, our licensees. For the brand and content suppliers we are a very attractive route to market, as manifested by the 20 new licensees we added to our client base in 2009.



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We began the year under review with just 3 branded games live and ended with 66. Whilst this is, in fact, lower than originally planned and was also skewed heavily towards the latter part of the year, we are confident that the roll out will continue to gain momentum in 2010. The 66 games rolled out thus far represent only about 35% of the games for which we have contracts.

During 2009, our licensee base rose from 14 to 32 and our expanded portfolio of branded games including:

*Superman*

*Wonder Woman*

*Batman*

*King Kong*

*Call of Duty*

*Streetfighter II*

In addition to those listed above we also launched a series of other in-house games that proved very popular. These included *Jenga*, *Samba Nights*, *Monkeys to Mars*, *Aces and Faces*, *Casinomeister*, *Millionaire's Club III* and *Roamin' Gnome*. Our goal is to continue to provide excellent game content supported by innovative game mechanics and bonuses.

### **NEW DEVELOPMENTS**

To lead the gaming industry has always been Cryptologic's aim. We are determined to maintain our proud track record of introducing new games to the market which people around the world want to play. That means always ensuring that the quality of our products and our customer support is second to none. It also means putting innovation at the center of everything we do.

An example of this is the unveiling of our new lobby for our Internet casino software, which represents a further important industry advance. Using the newest interactive technology, the lobby enables improved navigation and search, an updated jackpot counter, customized features that allow people to keep track of their favorite games, and a game suggestion engine to connect the player to other Cryptologic games. In all, the look and feel and the ease of use will add to the "stickiness" of the offering - a key element on any online business.

Cryptologic, through market awareness and focus groups, is acutely aware of the fact that the e-gaming market will continue to evolve rapidly in numerous ways. We know that social networking, peer-to-peer (one-to-one) gaming, 3D, mobile gaming, subscription gaming, games of skill, tournament and league-based gaming are all aspects of the future.

In order to address these demands we created the Cryptologic Center for Innovation. It is through this group that we were able to bring a new product to market, from concept to release, in four months - something that would, in the past, have taken up to 12 months.

As we move into 2010 we anticipate the launch of our first 3D games and also a game that will allow a player to play for fun, play for money, play against the house or play against a friend all in a single instance of the game.

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It is not just a question of being able to produce good games and game concepts but it is vital also to understand emerging technologies. In 2009, an investment of Cryptologic (in which we hold a minority interest) explored some of the cutting edge capabilities of the iPhone and through Warner Bros released a Harry Potter application which, using the accelerometer functions of the iPhone, allowed a dueling contest to take place phone to phone via Bluetooth or over the Internet. It is easy to see how the application of this capability can be used in dice based games such as craps or backgammon again, a technological segue into social networking and gaming.

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These are just a few examples of the technologies we intend to bring to the market.

We believe that the new business model, our creativity and innovative approach always looking into the future but executing day to day is the right one for the long-term growth of the Company.

## **OUTLOOK**

The global e-gaming industry experienced a downturn in 2009 and continues to face challenges early in 2010. According to Global Betting and Gaming Consultants, the market is expected to recover in the long term, and the size of the market (excluding North America) is set to rise from \$10.7 billion in 2008 to an estimated \$14.9 billion in 2012. Cryptologic is well placed to enhance its position in the industry but only if we stay focused and lean, and capable of responding to changing market expectations and delivering products and service levels of the highest quality.

We have been successful in 2009 in driving down the recurring cost base in the business by some \$20.6 million when compared to 2008. This has involved many difficult decisions, including reducing the workforce by 25%. Additionally, we have made changes to our operational infrastructure including a material reduction in the number of servers we operate. We have also reduced the number of data centers we utilize from 11 to 5. These changes, which have not affected productivity or service levels, have consolidated our infrastructure and were necessary in order to maintain competitiveness.

Looking forward, we believe the buoyant European market offers the greatest scope for growth. The UK market is mature and stable and, whilst its true to say the EU regulatory framework is still evolving, we remain convinced that Europe looks set to dictate the direction the industry takes in the period ahead. Our goals for 2010 are:

- Improved revenue from hosted casino as new licensees go live and existing licensees benefit from investment in major rebranding, a new lobby and advertising initiatives;

- Branded games continue to gain momentum with the annual run rate currently at \$5 million as more games come on stream;

- Number of new branded games launched by licensees to date and generating revenues currently at 93, with a backlog of approximately 115 games; and

- Costs expected to reduce further in 2010 as additional measures are implemented to manage overheads.

We continue to monitor conditions in Asia where the current regulatory environment represents a hurdle to progress. Longer term, however, such markets may provide some interesting opportunities for Cryptologic.

Whilst the US market has effectively been closed since the passing of the Unlawful Internet Gaming Enforcement Act in October 2006, there are some indications that the market may re-open. We continue to monitor the situation closely and are examining various options that would allow us re-entry at the appropriate time.

**A. OPERATING RESULTS**

**Comparison of 2009 and 2008**

**Revenue**

CryptoLogic recorded revenues for the year ended December 31, 2009 of \$39.8 million, a decline of 35.3% (2008: \$61.5 million).

Licensing fees and services from our casino licensees, both Internet casinos and Branded Games, are calculated as a percentage of a licensee's level of activity in its online casino site. Fees from online poker are based on a percentage of the licensee's rake per hand in regular or ring games (the rake is typically 5% of the pot, up to a maximum amount per hand) or fixed fees for entry into poker tournaments.

**Internet Casino**

Internet casino revenue decreased to \$30.0 million or 28.4% for the year ended December 31, 2009 (2008: \$41.8 million).

Fees or licensing revenue from our casino business is calculated as a percentage of a licensee's level of activity in its online casino site. This is affected by the number of active players on the licensee's site and their related gaming activity. In turn, these results are influenced by a number of factors such as the entertainment value of the CryptoLogic developed games, the frequency and success of new offerings and the effectiveness of the licensee's marketing programs. Internet casino revenue is also impacted by the relative strength of the U.S. dollar to both the euro and the British pound as our licensees provide online casinos in these currencies for which we earn a percentage that is translated into U.S. dollars, our functional currency.

This decrease in revenue is due to the stronger U.S. dollar in relation to both the euro and the British pound, general macro-economic conditions and poor performance of two of the Company's major licensees as well as a non recurring \$1.0 million benefit recorded in 2008 associated with a reduction in expected royalty payments. The relative strength of the U.S. dollar negatively impacted revenue by \$3.1 million. After normalizing for the impact of the strength of the U.S. dollar, Internet casino revenue decreased by approximately 21.0% in 2009. Partially offsetting these decreases was \$0.8million benefit from a revision of our estimate to discharge future jackpot payouts and a non recurring \$0.8 million benefit associated with the resolution of a commercial matter. The Company is liable for funding the jackpot wins from the pool of funds collected and accrues the jackpot amount. The Company regularly performs analysis of the accumulation of jackpot funds and amounts required to address jackpot payouts.

Internet casino licensing and associated support fees constitute our core revenue base, representing 75.3% of our total revenue in 2009 (2008: 68.0%). While casino fees declined in absolute dollars they have increased as a percentage of total revenue because of the success of new games and the decline in poker.

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We intend to continue delivering a succession of new product innovations, thereby generating additional activity and interest in our licensee sites. This in turn generates online licensee fees which will grow our casino business. While online casino fee revenue growth outside the U.S. is predicted to remain strong, we expect organic growth will be insufficient to return to the 2006 revenue base in the short term. Consequently we continue to aggressively explore other alternatives including new licensees to increase revenues and continue to control costs as we grow revenues outside of the U.S. and return to those levels of earnings.

### Internet Poker

Internet poker licensee fees declined 74.4% to \$3.5 million for the year ended December 31, 2009 (2008: \$13.8 million). The decrease in Internet poker revenue is primarily due to the transition of our poker network to

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GTECH, which reduced the number of the Company's poker licensees and increased fees paid to GTECH, the relative strength of the U.S. dollar and a decline in the overall poker industry. In March 2009, the Company completed its outsourcing of its hosted poker business to GTECH, which gives CryptoLogic's poker licensees and players access to a larger network at significantly lower cost to CryptoLogic. As expected, poker revenue declined as a small number of significant poker licensees did not migrate to GTECH and the fees that we earned were reduced by amounts paid to GTECH. The migration to the GTECH poker room has resulted in larger declines in poker revenue than expected. In 2009, the U.S. dollar was significantly stronger when compared to the euro and British pound when compared to the same period in 2008, negatively impacting poker revenue by approximately \$0.6 million. Poker fees were 8.8% of total 2009 revenue (2008: 22.4%).

### Branded Games

Branded games revenue was \$2.8 million for the year ended December 31, 2009 (2008: \$0.3 million). Branded games revenue accounted for 7.1% of total revenue in 2009 (2008: 0.5%). During the year, the Company's revenue producing games increased from 3 to 66 games at the end of the 2009. The majority of the games delivered were in the second half of the year including 20 games in the third calendar quarter and 33 games in the fourth quarter. The Company expects branded game revenue to increase in 2010 as it benefits from a full year of revenue on games delivered in 2009 and from increases in the number of revenue producing games.

Branded games revenue has a build once, license often model generating significant economies of scale and is delivered at a substantially lower cost than Internet casino revenue as the games are hosted and maintained directly by the licensee. The branded games are generally delivered by platform providers, at their own cost, and are then made available to our mutual customers. Once delivered, licensing revenue is calculated as a percentage of a licensee's level of activity in their online casino sites. Branded games revenue is affected by the number of active players on the licensee's site and their related gaming activity.

On March 30, 2010, the Company delivered to Marvel a Statement of Claim regarding an alleged breach by Marvel of certain provisions of its agreement with the Company relating to the licensing of Marvel comic book characters to CryptoLogic. Any proceeding flowing from the said Statement of Claim must proceed by way of arbitration in the City of New York and under New York law, as per the contract with Marvel.

During 2009, the Company continued to expand its portfolio of branded content including securing additional royalty rights with DC Comics, a division of Warner Bros., for the use of *Batman*, *Superman* and *Wonder Woman*, among others and with Paramount Digital Entertainment for a collection of approximately 20 feature films. Including these additional royalty rights into our portfolio, which also includes Marvel characters, *King Kong*, *Jenga* and *Bejeweled*, will allow the Company to strengthen ongoing interest in its products, allow it to expand its licensees for both Internet Casino and branded games and better allow its licensees to attract customers to their respective sites.

### Other Revenue

Other revenue, which includes fees for software customization, advertising and marketing services generated from our portal business and fees associated with our ecash business, decreased to \$3.5 million or 37.4% (2008: \$5.6 million). The decrease in other revenue is primarily due to a decrease in software customization due to timing of completion of certain projects and decreased advertising services associated with our portals business. Offsetting this decrease was an increase in ecash recoveries. Other revenues accounted for 8.8% of total revenue (2008: 9.1%).

### International Diversification

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CryptoLogic's global strategy has resulted in a geographically-diversified business intended to mitigate the risks of ongoing legislative uncertainty in various countries, by increasing exposure to gaming-friendly jurisdictions like the U.K., and benefiting from near-term growth opportunities in overseas markets.

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Our ability to succeed in these markets depends on our licensee roster, which includes some of the most respected names in European gaming. The United Kingdom's 2005 enactment of a law to regulate online gaming continues to foster favorable growth and increased competition in the Internet gaming industry, for our customers and for CryptoLogic. With the relocation of all licensee operations to Malta, a member of the European Union, access to the European markets is strengthened. CryptoLogic continues to build partnerships, develop products, and pursue new markets.

#### Recurring Revenue

CryptoLogic's licensee fees reflect a revenue model based on building long-standing relationships with customers. In 2009, 91.2% (2008: 90.9%) of CryptoLogic's fee revenue was generated from software licensing and services contracts that generate recurring revenue.

#### **Expenses**

Consistent with prior years, during 2009 we incurred expenses in five categories: operating, general and administrative, reorganization charges, finance and amortization. Additionally, due to several factors including the decision to merge its poker room and macro-economic factors, the Company has recorded poker room integration costs, asset impairments and impairment of goodwill.

In 2009, total expenses decreased 22.1% to \$77.6 million (2008: \$99.6 million) primarily due to the impact of our cost reduction program which reduced operating and general and administrative expense. Offsetting these decreases were impairments of assets and impairment of goodwill. In 2009, the Company recorded approximately \$24.8 million in non-recurring charges, of which approximately \$3.0 million represents future cash outlays primarily on lease termination costs in Toronto and employee severance.

We continue to focus on maintaining close control over all discretionary expenditures as we align to the new market environment. We expect our costs to decrease in absolute terms in 2010, as we execute on the reorganization plan announced in Q4 2008 and expanded in Q4 2009.

#### *Operating Expense*

CryptoLogic's operating expense comprises development and support expense, which includes all personnel costs, equity compensation costs for employee stock options, licensee support, marketing, e-cash systems and support costs, customer service expense, and expenses related to regulatory compliance.

Costs associated with software development are expensed as incurred unless costs meet the criteria for deferral and amortization under Canadian Generally Accepted Accounting Principles (Canadian GAAP).

In 2009, operating expense decreased by 28.4% or \$15.8 million to \$39.9 million (2008: \$55.6 million). In 2009, operating expenses were 100.2% of revenue (2008: 90.4%). The decrease in operating expense was primarily due to the Company's cost reduction program executed in connection with its reorganization plan, which included outsourcing the poker room to GTECH, reduced headcount and related costs, consulting costs and IT infrastructure costs. Operating expense also benefited from decreased ecash processing fees resulting from renegotiation of its contract terms and lower deposit levels due primarily to the migration of poker to GTECH as well as reduced marketing program related costs that we share with certain licensees. Operating costs have also benefitted by the strengthening of the U.S. dollar, which reduced operating expenses by \$3.3 million in 2009. A strong U.S. dollar is generally favorable on expenses as they are generally denominated in Canadian dollars, euro and British pounds. Operating expense in 2009 also benefited from more active management of risks associated with foreign exchange

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movements. In 2008, the Company recorded a \$6.1 million loss on foreign exchange and there was no similar loss recorded in 2009. Offsetting these decreases were increased investment in software development capability in lower cost jurisdictions.

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We must continue our investment in our core product and services to help licensees grow market share and player loyalty despite the reduction in revenue. Consequently we have gaming capacity for additional licensee fees that we are aggressively looking to fill.

At December 31, 2009, CryptoLogic had 211 employees dedicated to implementing our strategy in a competitive and increasingly sophisticated market, down from 276 a year earlier.

### *General and Administrative Expense*

General and administrative (G&A) expense includes overhead and administrative expense, travel expense and professional fees relating to our business development, infrastructure and public company listings.

In 2009, G&A expense was \$10.2 million or 25.6% of revenue (2008: \$13.7 million or 22.2%).

The decrease in G&A expense in 2009 as compared with 2008 is a result of decreased professional fees associated with our annual audit and compliance with Sarbanes Oxley, reduced expenses for tax planning, and decreased consulting fees associated with the protection of our intellectual property. G&A expense was also positively impacted by decreased occupancy costs due to subleasing certain vacant office space.

### *Reorganization Charges*

In November 2008, we announced a plan for reorganization of our business focused on reducing costs by outsourcing non core activities, including integrating its poker network with one of the world's leading gaming technology and services companies, transitioning certain functions to lower cost jurisdictions and eliminating certain redundant functions. Due to continued unfavorable macro-economic conditions and lower revenue than expected, we expanded our reorganization plan and will outsource additional technology infrastructure activities, consolidate additional data centre operations, and migrate additional functions to lower cost jurisdictions. This reorganization plan will result in further reductions in headcount related costs, lease termination costs due to a reduction of our leased office space in both Canada and Cyprus, and associated asset impairments. Reorganization expense recorded in 2009 was \$7.1 million and comprises professional fees required to execute the plan of \$1.1 million, severance of \$1.1 million, lease termination costs associated with the office space in Canada of \$1.8 million and associated asset impairments of \$3.1 million. The Company expects further cash outlays of \$3.0 million, primarily on lease termination costs in Toronto and employee severance, to fully execute the restructuring plan.

### *Amortization*

Amortization expense is based on the estimated useful lives of the assets and includes the amortization of our investments in computer equipment, leasehold improvements, software licenses, and intangible assets to support our business activities.

Amortization expense was \$4.9 million, or 12.2% of revenue (2008: \$5.9 million or 9.6%). The decrease in amortization reflects lower investments in computer equipment, and software licenses and the impact of asset write downs completed in Q4 2008.

### *Poker-Room Integration Costs*

During 2008, the Company announced its plans to integrate our poker operations with a third party poker network. Accordingly the Company identified certain assets including software development projects and certain program costs where their carrying value exceeded the fair value of these assets. Poker room integration costs include poker related program costs of \$2.5 million as well as the write off of in process software development projects of \$0.4 million and other costs of \$0.2 million.



*Asset Impairments*

The Company regularly reviews its assets for impairment. During 2009, the Company reviewed its long term investments and noted various indicators of impairment including significant financial difficulty, restructuring activities and limited ability to operate a profitable business in the short and medium term. Furthermore, our book value was significantly in excess of our market capitalization, which was a further indication that our long-term investments may be impaired. Consequently, the Company determined that the carrying value of its long term investments in Mobilebus, Mikoishi, Jingle and 568 Inc. were greater than their respective fair values resulting in an impairment charge of \$6.3 million. The fair value of the investments was determined by discounting expected net future cash flows. The Company also reviewed certain software development projects as a result of difficult macro-economic conditions and a decline in expected future revenues, which resulted in an impairment charge of \$2.7 million.

During 2008, the Company determined that the carrying values of certain software development projects and intangible assets exceeded their fair value and recorded a charge of approximately \$6.7 million and \$7.2 million, respectively. Furthermore, the Company determined that the carrying value of its investment in Mikoishi, a game developer located in Singapore, was greater than its fair value and recorded a \$2.2 million charge.

*Impairment of Goodwill*

Goodwill is not amortized and is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. During the year, the results of the portals business were below expectations and the book value of the Company was significantly in excess of its market capitalization, which were both indications that the value of its goodwill was impaired. The fair value of the goodwill was determined by discounting expected net future cash flows of the portals business. As a result, the Company decided that the carrying value of the goodwill exceeded its fair value and recorded an impairment charge of \$6.5 million.

*Departure Costs of Former CEO*

In February 2008 the former President and CEO departed the Company. The Company recorded an associated charge of approximately \$3.4 million which included departure payments of approximately \$2.9 million and related professional fees of \$0.5 million.

*Interest Income*

Interest income, comprising interest earned on cash and short term investment balances, declined to \$0.4 million in 2009 (2008: \$2.1 million). The decrease was as a result of lower cash balances due primarily to cash used in operating activities and lower interest rates earned on cash deposits.

*Provision for Income Taxes*

In 2009, despite large operating losses, we recorded an income tax expense of \$1.1 million (2008: net benefit of \$0.5 million) as the impairments of our long term assets, goodwill and certain asset impairments associated with our restructuring are not immediately deductible for tax purposes and in some cases may never be deductible. The tax expense recorded in 2009 is also impacted by a \$2.2 million impairment of future tax assets accumulated in jurisdictions where recoverability is no longer probable. The recoverability of the future tax assets is no longer considered probable due to expected changes in the corporate structure which will reduce operations in certain jurisdictions where losses had accumulated. Offsetting this tax expense is a benefit of \$1.7 million recorded in the first quarter of 2009.

The tax benefit of \$1.7 million recorded in the first quarter of 2009 is primarily a result of recent amendments to Section 261 of the Income Tax Act in Canada that permit certain corporations resident in Canada to elect to determine their Canadian tax amounts in the corporation's functional currency as opposed to the

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general requirement that all amounts that are relevant to the computation of tax under the Canadian Income Tax Act be in Canadian dollars. This change resulted in a benefit to income tax of approximately \$1.4 million in the first quarter of 2009. The Company recorded an additional benefit of approximately \$0.3 million based on the actual tax return filed.

CryptoLogic is subject to tax in many jurisdictions. The Company is actively working to reduce the number of its subsidiaries, which will reduce the overall tax burden. The consolidated net operating loss is composed of operating losses in some jurisdictions and operating profits in others which results in a tax expense despite material consolidated net losses. Subject to significant changes in the tax rates of those jurisdictions or significant changes in our corporate structure, we generally expect a blended tax rate of approximately 15%, once we return to profitability.

### *Minority Interest*

Pursuant to a business reorganization completed in 2007 (the Arrangement), CryptoLogic acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement became an indirect subsidiary of CryptoLogic. As part of the Arrangement, the Company issued to shareholders of CryptoLogic Inc. either an equivalent amount of common shares of the Company or, in the case of taxable Canadian residents, exchangeable shares (Exchangeable Shares) of CryptoLogic Exchange Corporation (CEC), an indirect subsidiary of the Company. The Exchangeable Shares are, as nearly as practicable, the economic equivalent of CryptoLogic's common shares. The Exchangeable Shares participate equally in voting and dividends with the shareholders of the Company. No additional Exchangeable Shares have been or will be issued. For more information, see the Management Information Circular dated April 23, 2007 available on [www.sedar.com](http://www.sedar.com). For accounting purposes, the Arrangement has been accounted for using the continuity of interest method, which recognizes the Company as the successor entity to CryptoLogic Inc. Accordingly, financial information reflects the financial position, results of operations and cash flows as if the Company has always carried on the business formerly carried on by CryptoLogic Inc., with all assets and liabilities recorded at the carrying values of CryptoLogic Inc. The interest held by CEC shareholders has been presented as a minority interest in the consolidated financial statements, as required under Canadian GAAP.

The common shares of the Company owned by CEC are considered a non-controlling interest of the Company for accounting purposes only and consequently, a proportional amount of the net earnings before minority interest is recorded as minority interest.

Minority interest will continue until all Exchangeable Shares have been exchanged into common shares of the Company or until June 1, 2014 when CEC will redeem all outstanding Exchangeable Shares in return for common shares of the Company.

### *Net (Loss)/Earnings*

CryptoLogic recorded a net loss of \$35.5 million for the twelve months ended December 31, 2009 as compared with net loss of \$32.7 million for the same period in 2008. The net loss was primarily due to decreased poker and casino revenues, and \$24.8 million in non recurring charges consisting of impairments of long term investments, reorganization costs including severance costs, costs to exit lease obligations and the write off of associated capital assets, impairment of future tax assets, and the impairment of goodwill. The non-recurring charges include approximately \$3.0 million representing future cash outlays primarily on lease termination costs in Toronto and employee severance. Offsetting these amounts were increased revenue from Branded Games and decreased operating and G&A expenses.

### *Foreign Exchange*

Our financial results are reported in U.S. currency, which is subject to fluctuations in respect of the currencies of the countries in which we operate, including British Pounds, euro, and Canadian Dollars. Accordingly, fluctuations in the exchange rate of world currencies could have a positive or negative effect on our



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reported results. We may utilize a hedging program from time to time and/or take advantage of the natural hedge in having operations in multiple currencies to mitigate a portion of our currency risks, but there can be no assurance that we will not experience currency losses in the future, which could have a material adverse effect on our business, revenues, operating results and financial condition.

In 2009, the Company recognized a total foreign exchange loss of \$0.3 million (2008: \$6.2 million, 2007: foreign exchange gain of \$0.68 million), which is recorded as an operating expense in the accompanying consolidated statements of earnings.

### *Government Regulation*

On October 13, 2006, the U.S. enacted the UIGEA, which effectively banned online gaming in that country by making it illegal to process related financial transactions. The industry-wide impact of UIGEA has negatively affected our business by significantly reducing our revenue and earnings. Similar prohibition legislation may be adopted in other jurisdictions.

While the U.K. and other European countries such as Malta and Gibraltar are adopting a regulated online gaming approach, opposing views are developing in Europe. Some European countries, including Italy, Germany and France are taking action aimed at banning foreign online gaming operators, in many cases to protect state sponsored monopolies. The European Commission has commenced infringement proceedings against some member states that are taking a protectionist approach a development that we believe is favorable to the industry in Europe. While most decisions rendered by the ECJ over the past several years have been favorable to the industry, the court has been careful to confirm, most recently in the *Santa Casa* decision related to the Portuguese market, that state sponsored monopolies may be established in compliance with EU treaty law, if done so in the appropriate manner and for the appropriate reasons.

There can be no assurance that legislation prohibiting Internet gaming or regulating various aspects of Internet gaming or the Internet gaming industry will not be proposed and passed in potentially relevant jurisdictions. The burden of compliance with any such legislation may have a material adverse effect on our business, financial condition and results of operations.

### **Comparison of 2008 and 2007**

#### Revenue

CryptoLogic recorded revenues for the year ended December 31, 2008 of \$61.5 million, a decline of 16.5% (2007: \$73.7 million).

Licensing fees and services from our casino licensees are calculated as a percentage of a licensee's level of activity in its online casino site. Fees from online poker are based on a percentage of the licensee's rake per hand in regular or ring games (the rake is typically 5% of the pot, up to a maximum amount per hand) or fixed fees for entry into poker tournaments.

#### *Internet Casino*

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Internet casino fee revenue decreased to \$42.2 million or 14.7% for the year ended December 31, 2008 (2007: \$49.5 million).

Fees or licensing revenue from our casino business is calculated as a percentage of a licensee's level of activity in its online casino site. This is affected by the number of active players on the licensee's site and their related gaming activity. In turn, these results are influenced by a number of factors such as the entertainment value of the CryptoLogic developed games, the frequency and success of new offerings and the effectiveness of the licensee's marketing programs. Internet casino revenue is also impacted by the relative strength of the U.S. dollar

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to both the euro and the British pound as our licensees provide online casinos in these currencies for which we earn a percentage that is translated into U.S. dollar, our functional currency.

In 2008, Internet casino fee revenue benefited from a \$1.0 million reduction in expected royalty payments. In 2007, Internet casino fee revenue benefited from two non-routine items recorded during the year, a revision of our estimate to discharge future jackpot payouts of \$4.5 million as well as a \$2.0 million reduction in our accrual for contingencies. After normalizing for these items, Internet casino revenue decreased by approximately 4.2% in 2008. This decrease in revenue is due to the stronger U.S. dollar in relation to both the euro and the British pound, the poor performance of a major licensee as well as general macro-economic conditions which primarily impacted the final quarter of fiscal 2008. The decrease in revenue is offset in part, by efforts to replace the business lost due to the passage in the U.S. of the Unlawful Internet Gambling Enforcement Act ( UIGEA ) by expanding in other markets primarily continental Europe and the successful release of its newest line-up of casino games.

Internet casino licensing and associated support fees constitute our core revenue base, representing 68.5% of our total revenue in 2008 (2007: 67.1%). While casino fees declined in absolute dollars they have increased as a percentage of total revenue because of the success of new games and the decline in poker.

We intend to continue delivering a succession of new product innovations, thereby generating additional activity and interest in our licensee sites. This in turn generates online licensee fees which will grow our casino business. While online casino fee revenue growth outside the U.S. is predicted to remain strong, we expect organic growth will be insufficient to return to the 2006 revenue base in the short term. Consequently we continue to aggressively explore other alternatives including new licensees to increase revenues and continue to control costs as we grow revenues outside of the U.S. and return to record levels of earnings.

### *Internet Poker*

Poker fees remain a significant revenue contributor to the overall revenue of CryptoLogic at 22.4% of total 2008 revenue (2007: 26.5%). However, our Internet poker licensee fees declined to \$13.8 million or 29.2% (2007: \$19.5 million) primarily due to a slowing of growth in European poker.

CryptoLogic offers a virtual central poker room for its licensees. Fees from online poker are based on a percentage of the licensee's rake per hand in regular or ring games (the rake is typically 5% of the pot, up to a maximum amount per hand), or fixed entry fees for entry into poker tournaments. Online poker revenue is also impacted by the relative strength of the U.S. dollar to both the euro and the British pound as our licensees provide online casinos in these currencies for which we earn a percentage that is translated into U.S. dollar, our functional currency. Players prefer poker rooms with strong liquidity rooms that offer high availability of games at the desired stake levels, in their currency of choice, on a 24/7 basis. During the year, the Company announced plans to merge its major poker customers into a third party international poker network during the first quarter of 2009. We expect this integration to decrease poker revenues in absolute terms, but decrease costs associated with delivering poker revenues at a greater rate.

### *Other Revenue*

Other revenue increased to \$5.6 million or 19% (2007: \$4.7 million), which included fees for software customization and advertising and marketing services generated from our portal business. The increase in other revenue is primarily due to a \$1.2 million benefit associated with a review of our e-cash operations, which resulted in a reduction in expected future payments as well as increased advertising revenues associated with our portal business due to the acquisition of casino.co.uk. Partially offsetting these increases were fewer commerce based transactions. Other revenues accounted for 9.1%



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### *Recurring Revenue*

CryptoLogic's strong recurring licensee fees reflect the strength of a revenue model based on building long-standing relationships with premium customers. In 2008, 90.9% (2007: 93.6%) of CryptoLogic's fee revenue was generated from software licensing and services contracts that generate recurring revenue.

During 2008, we began licensing individual branded games to leading online gaming companies and have secured several contracts which we will earn revenue on a revenue share basis. During 2009, the Company expects to complete the deployment of the games and is expected to generate significant revenue in 2009 and beyond. In addition, we have secured additional royalty rights including arrangements with DC Comics for the use of *Batman* and *Superman* and with Paramount Digital Entertainment for a collection of approximately 20 feature films. These additional royalty rights will provide ongoing interest in products, and better allow our licensees to attract customers.

### *Seasonality*

Historically, the Group has experienced seasonality with slower sales in the second and third quarters, as the use of the Internet is not as strong in the summer months when players tend to spend less time indoors and at their computers. Historically, the first and fourth quarters (during the winter and autumn seasons) have been the strongest revenue periods.

### Expenses

Consistent with prior years, during 2008 we incurred expenses in five categories: operating, general and administrative, reorganization charges, finance and amortization. Additionally, due to several factors including the Company's decision to merge its poker room and macro-economic factors, the Company has recorded poker room integration costs, impairments of long term assets and departure costs associated with the Company's former CEO.

Total expenses increased to \$99.6 million or 37.6% (2007: \$72.4 million) primarily due to charges recorded in 2008 for impairments of long-term assets (\$16.1 million), poker room integration costs (\$3.1 million), departure costs associated with our former CEO (\$3.4 million) as well as increased operating and general and administrative costs.

We continue to focus on maintaining close control over all discretionary expenditures as we align to the new market environment. We expect our costs to decrease in absolute terms substantially in 2009, as we execute on the reorganization plan announced in November 2008 where we expect to decrease recurring costs between \$12 million to \$15 million.

### *Operating Expense*

CryptoLogic's operating expense comprises development and support expense, which includes all personnel and equity compensation costs for employee stock options and long-term incentive program; licensee support; e-cash systems and support costs; customer service expense; and expense related to regulatory compliance.

Development costs are expensed as incurred unless costs meet the criteria for deferral and amortization under generally accepted accounting principles.

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Total operating expense was \$55.6 million, or 90.4% of revenue (2007: \$49.4 million or 67.1%). The increase in operating expense was primarily due to approximately \$6.1 million loss on foreign exchange recorded during the third and fourth quarters as the U.S. dollar appreciated by approximately 34% against the British pounds and 12% against the euro when the Company had significant net asset positions in these currencies. Other contributing factors to the increased operating expense for the twelve months ended December 31, 2008 when

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compared to the same period of the prior year were increased consulting costs and marketing costs, as the Company focused on adding to its developmental capacity and increasing its marketing activity in new and existing markets. Operating expense in 2008 was favorably impacted by reduced compensation, reduced costs recorded in connection with the Company's long-term incentive plan, and e-cash processing fees. The reduced cost associated with the Company's long-term incentive plan was due to revised expectations on the probability of meeting the respective targets.

We must continue our investment in our core product and services to help licensees grow market share and player loyalty despite the reduction in revenue. Consequently we have gaming capacity for additional licensee fees that we are aggressively looking to fill.

At December 31, 2008, CryptoLogic had 276 employees dedicated to implementing our strategy in a competitive and increasingly sophisticated market, down from 310 a year earlier.

### *General and Administrative Expense*

General and administrative (G&A) expense includes overhead and administrative expense, travel expense and professional fees relating to our business development, infrastructure and public company listings.

In 2008, G&A expense of \$13.7 million represented 22.2% of revenue (2007: \$10.2 million or 13.8%), an increase both as a percentage of revenue and in absolute dollars.

The increase in G&A expense in 2008 as compared with 2007 is a result of increased professional fees associated with our annual audit and compliance with Sarbanes Oxley, additional expense for tax planning, increased fees for advice for merger and acquisition opportunities and consulting fees associated with the protection of our intellectual property. G&A expense was also negatively impacted by increased occupancy costs associated with the establishment of our executive headquarters in the Republic of Ireland.

### *Reorganization Charges*

In November 2008, the Company announced plans to merge its poker network with one of the world's leading gaming technology and services companies. Accordingly the Company has recorded a charge of \$1.4 million primarily comprising of severance costs and professional fees.

In 2007, the Company recorded reorganization charges associated with our establishment of the executive headquarters in the Republic of Ireland and the restructuring of the organization during the year. In 2007, such costs totaled \$5.7 million or 7.7% of revenue and primarily comprise professional fees and expenses related to employee relocation and severance.

### *Amortization*

Amortization expense is based on the estimated useful lives of the assets and includes the amortization of our investments in computer equipment, leasehold improvements, software licenses, and intangible assets to support our business activities.

Amortization expense was \$5.9 million, or 9.6% of revenue (2007: \$6.6 million or 8.9%). The decrease in amortization reflects lower investments in computer equipment, and software licenses offset by a full year of amortization of purchased intangibles for casino.co.uk and Parbet.com.

### *Poker-Room Integration Costs*

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During 2008, the Company announced its plans to integrate our poker operations with a third party poker network. Accordingly the Company identified certain assets including software development projects and certain program costs where their carrying value exceeded the fair value of these assets. Poker room integration costs

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include poker related program costs of \$2.5 million as well as the write off of in process software development projects of \$0.4 million and other costs of \$0.2 million.

### *Impairments of Long-Term Assets*

The Company regularly reviews its assets for impairment. During 2008, the Company determined that the carrying values of certain software development projects and intangible assets exceeded their fair value and took a charge of approximately \$6.7 million and \$7.2 million, respectively. Furthermore, the Company determined that the carrying value of its investment in Mikoishi, a game developer located in Singapore, was greater than its fair value and recorded a \$2.2 million charge.

### *Departure Costs of Former CEO*

In February 2008 the former President and CEO departed the Company. The Company has recorded a charge of approximately \$3.4 million associated which included departure payments of approximately \$2.9 million and related professional fees of \$0.5 million.

### *Interest Income*

Interest income, comprising interest earned on cash and short term investment balances, declined to \$2.1 million in 2008 (2007: \$6.2 million). The decrease was as a result of lower cash balances due primarily to cash used in operating activities and lower interest rates earned on cash deposits.

### *Provision for Income Taxes*

Income taxes were a benefit of \$0.5 million (2007: expense of \$1.0 million), and were net of a future income tax recovery. The decrease in 2008 primarily resulted from lower revenues and losses recognized. Changes in future income taxes result from differences between tax and accounting recognition with respect to certain of CryptoLogic's expenses.

CryptoLogic is subject to tax in many jurisdictions. Subject to significant changes in the tax rates of those jurisdiction or significant changes in our corporate structure, the Company generally expects a blended tax rate of approximately 15%.

Recent and proposed amendments to Section 261 of the Income Tax Act in Canada permit certain corporations resident in Canada to elect to determine their Canadian tax amounts in the corporation's functional currency as opposed to the general requirement that all amounts that are relevant to the computation of tax under the Canadian Income Tax Act be in Canadian dollars. As at December 31, 2008 the amending legislation had not met the requirement of being substantively enacted for purposes of Canadian generally accepted accounting principles. Accordingly, the effects of the October 2008 election have not been incorporated in the accompanying consolidated statements of earnings and comprehensive income for the year ended December 31, 2008. We expect this amendment to become law in the first quarter of 2009, which will allow us to record a benefit to income tax of approximately \$1.4 million. We are subject to Canadian GAAP but taxes are based on the local rules and laws. So not all of our subsidiaries are either resident in Canada and would pay the tax based on their local jurisdiction.

### *Minority Interest*

Pursuant to a business reorganization implemented by way of an Ontario, Canada Superior Court of Justice approved plan of Arrangement and approved by the shareholders on May 24, 2007, the Company acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement became an indirect subsidiary of the Company. As part of the Arrangement, the Company issued either an equivalent amount of common shares of the Company or, in the case of taxable Canadian residents, Exchangeable Shares of CEC, an indirect subsidiary of the Company.

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The common shares of the Company owned by CEC are considered a non-controlling interest of the Company for accounting purposes only and consequently, a proportional amount of the net earnings before minority interest associated with subsidiaries directly or indirectly owned by CEC is recorded as minority interest.

Minority interest will continue until all Exchangeable Shares have been exchanged into common shares of the Company or until June 1, 2014 when CEC will redeem all outstanding Exchangeable Shares in return for common shares of the Company.

### *Net (Losses)/Earnings*

CryptoLogic recorded a loss of approximately \$32.7 million for the twelve months ended December 31, 2008 as compared with net income of \$5.5 million for the same period in 2007. The decrease in profitability for the year ended December 31, 2008 as compared with the same period of the previous year was due to impairments of intangible assets associated with the Parbet acquisition, adjustments to the carrying value of certain software development projects, costs associated with the integration of our poker room with a third party network, departure costs associated with our former CEO, reorganization charges and declines in casino and poker revenue.

## **B. LIQUIDITY AND CAPITAL RESOURCES**

CryptoLogic remained debt-free in 2009 and remained highly liquid as our balance sheet at December 31, 2009 had net cash of \$23.7 million (2008: \$43.8 million). With the available cash resources we continue to have the financial strength and flexibility to continue to take advantage of opportunities in our markets and consider potential strategic acquisitions. Historically, we have also used cash resources to pay dividends and repurchase shares under the normal course issuer bid.

### **Comparison of 2009 and 2008**

At December 31, 2009, CryptoLogic ended the year with \$23.7 million of net cash (comprising cash and cash equivalents, restricted cash and security deposits) or \$1.71 per diluted share (December 31, 2008: \$43.8 million or \$3.15 per diluted share). Included in the cash balance is \$3.0 million of cash collected from licensees to pay winners of the Company's cumulative jackpot game offerings (2008: \$3.2 million). The decrease in net cash of \$20.1 million is primarily due to cash impact of operating losses (\$10.2 million), dividends paid (\$1.4 million), increase in prepaid assets (\$2.6 million) due primarily to payments to royalty providers including DC Comics, Marvel and Paramount offset by amortization, increase in accounts receivable (\$1.8 million) due primarily to the outsourcing of the poker network and the increase in branded games which each have a one month delay in cash settlement, a decrease in accounts payable and accrued liabilities (\$5.2 million) due to decrease in activity consistent with a cost reduction plan, capital expenditures (\$0.4 million), and investments in Asia (\$0.5 million). These decreases are offset by net tax refunds of \$2.0m. CryptoLogic continues to be debt free.

We pledge \$0.3 million in a security deposit at year end (2008: \$0.3 million). We maintain security on deposits as collateral granted to banks and payment processors that process deposit transactions on our behalf.

We are no longer required to maintain a deposit to support a letter of credit to the Lottery Gaming Authority of Malta to support user funds on deposit (2008: \$5.0 million).

At December 31, 2008, we were required to maintain a deposit of \$2.2 million that would have been paid to the Company's former CEO if there had been a change in control of the Company prior to April 30, 2009. There were no such amounts at December 31, 2009.

Operating Activities

Cash flow used in operating activities was \$17.8 million for the year ended December 31, 2009. (2008: \$18.6 million). Several factors contributed to the decrease in cash flow from operating activities from the prior year including, but not limited to:

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losses from operations primarily due to reduced revenues impacting cash by \$10.2 million; and working capital movements of \$7.6 million associated with increase in accounts receivable, payments to royalty providers, payments of accounts payable and accrued liabilities including amounts for reorganization of our business, offset in part by net tax refunds.

### Financing Activities

In 2009, \$1.4 million was used for financing activities (2008: \$6.7 million) due to dividends paid of \$1.4 million.

Cryptologic did not declare a dividend for the fourth quarter 2009 and will not declare any dividends in the short-term.

### Investing Activities

Investing activities provided \$6.3 million in 2009 (2008: \$6.2 million). The cash provided by investing activities was due to a reduction in restricted cash of \$7.2 as the Company reduced the amount to be maintained to support a letter of credit to the Lottery Gaming Authority of Malta to support user funds, offset by capital expenditure of \$0.4 million primarily associated with infrastructure improvement and investments in Jingle Inc. and Mikoishi of \$0.5 million.

### Working Capital

CryptoLogic's working capital at December 31, 2009 was \$26.5 million or \$1.91 per diluted share (December 31, 2008: \$41.2 million or \$2.97 per diluted share).

In the foreseeable future, we expect our cash needs to be funded through existing cash resources and operating cash flow. Our liquidity gives us the financial flexibility to continue to invest in our business and take advantage of opportunities in our markets and consider potential strategic acquisitions. Historically, our liquidity has also allowed us to pay dividends and repurchase shares under the normal course issuer bid.

### User Funds Held on Deposit

User funds held on deposit decreased 26.8% to \$7.9 million at December 31, 2009 (2008: \$10.8 million). The decrease in user funds is due primarily to the reduction in our poker business.

### Capitalization

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Since inception, CryptoLogic has had neither debt nor unutilized credit facilities. At December 31, 2009, CryptoLogic had 12,794,020 common shares outstanding and 563,521 stock options outstanding. The 12,794,020 outstanding common shares excludes 1,025,031 (2008: 1,090,974) exchangeable shares in CryptoLogic Exchange Corporation ( CEC ) which are entitled to be exchanged on a one-for-one basis for common shares of the Company. Including the exchangeable shares of CEC, the outstanding common shares of the Company would be 13,819,051 (2008: 13,819,051). As of March 11, 2010 there were 12,798,120 common shares of CryptoLogic outstanding and 1,020,931 exchangeable shares in CEC outstanding.

As part of the 2007 reorganization, Canadian residents received Exchangeable Shares of CEC, an indirect subsidiary of CryptoLogic. The Exchangeable Shares are, as nearly as practicable, the economic equivalent of common shares of CryptoLogic. For accounting purposes, the acquisition is accounted for using the continuity of interest method, which recognizes CryptoLogic as the successor entity to CryptoLogic Inc. The Exchangeable Shares can be exchanged for an equivalent amount of common shares of the Company at anytime and are accounted for as a minority interest. On June 1, 2014, CryptoLogic through its subsidiaries will redeem not less than all of the then outstanding Exchangeable Shares for an amount per share equal to the redemption price. The

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redemption price will be satisfied through the issuance and delivery of one common share of CryptoLogic for each Exchangeable Share. CryptoLogic has issued a special voting share to a third party trustee, the purpose of which is to provide holders of Exchangeable Shares with the right to vote on matters to be voted on by CryptoLogic shareholders. All outstanding options of CryptoLogic Inc. as of the date of the Arrangement were fully assumed by CryptoLogic under the same terms and conditions as originally granted by CryptoLogic Inc. The Exchangeable Shares provide those shareholders with the same voting and dividend rights as the common shares of CryptoLogic. No additional Exchangeable Shares will be issued and all stock options will give rise to the issue of additional common shares of CryptoLogic.

From December 3, 2008 to December 2, 2009, CryptoLogic has, through its Normal Course Issuer Bid, authorization to repurchase up to 1,267,871 common shares, under which we did not buy back any common shares. Under the 2007 Normal Course Issuer Bid, we repurchased and cancelled 124,905 common shares during 2008 for a total cost of \$1.4 million.

### **Comparison of 2008 and 2007**

CryptoLogic remained debt-free in 2008 and remained highly liquid as our balance sheet had net cash of \$43.8 million (2007:\$77.5 million). With the available cash resources we continue to have the financial strength and flexibility to continue our growth strategy, pay dividends, repurchase our own common shares through issuer bids and consider acquisition opportunities as they arise.

At December 31, 2008, CryptoLogic ended the year with \$43.8 million of net cash (comprising cash and cash equivalents, restricted cash and security deposits) or \$3.15 per diluted share (December 31, 2007: \$77.5 million or \$5.57 per diluted share). The decrease in net cash of \$33.7 million is primarily due to the dividends paid of \$5.4 million, repurchase of common shares under the Normal Course Issuer Bid of \$1.4 million, capital expenditures of \$4.5 million, investments in Asia of \$2.7 million, earn out payment with casino.co.uk of \$1.3 million, tax payments of \$4.8 million and operating losses offset in part by a decrease in restricted cash. CryptoLogic continues to be debt free.

We pledge \$0.3 million in a security deposit at year end (2007: \$1.5 million). We maintain security on deposits as collateral granted to banks and payment processors that process deposit transactions on our behalf.

We are also required to maintain a deposit of \$5.0 million (2007: \$20.0 million) to support a letter of credit to the Lottery Gaming Authority of Malta to support user funds on deposit.

At December 31, 2008, we were required to maintain a deposit of \$2.2 million that would have been paid to the Company's former CEO if there had been a change in control of the Company prior to April 30, 2009.

### Operating Activities

Cash flow used in operating activities was \$18.6 million for the year ended December 31, 2008. (2007: \$11.9 million). Several factors contributed to the decrease in cash flow from operating activities from the prior year including, but not limited to:

- losses from operations primarily due to reduced revenues and realized losses on foreign exchange;
- departure costs associated with the termination of the Company's CEO; and

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working capital movements of \$10.4 million associated with payments of tax and other liabilities.

### Financing Activities

In 2008, \$6.7 million was used for financing activities (2007: \$2.8 million) primarily for repurchases of common shares under the Normal Course Issuer bid of \$1.4 million and dividends paid of \$5.4 million

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While each future quarterly dividend is subject to Board approval based on our financial results for that particular period and the Board's view from time to time on the optimal uses of cash, we expect to continue paying dividends on a regular basis. However, as noted above, during 2009, we should start to trend toward quarterly revenue run rates similar to those realized prior to the UIGEA enactment, and continue to strive for net margins (net earnings as a percentage of revenue) in excess of 20%.

### Investing Activities

Investing activities provided \$6.2 million in 2008 (2007: cash used in investing activities of \$6.8 million). The increase in cash provided by investing activities was due to reductions in restricted cash and security deposits of \$14.7 million as the Company reduced the amount to be maintained to support a letter of credit to the Lottery Gaming Authority of Malta to support user funds, offset by capital expenditure of \$4.5 million primarily associated with infrastructure improvements and the Company's relocation of its HQ to Dublin, Ireland and investments in Jingle Inc., 568 and Mobilebus of \$2.7 million as the Company executes on its expansion plans in Asia.

### Working Capital

CryptoLogic's working capital at December 31, 2008 was \$41.2 million or \$2.97 per diluted share (December 31, 2007: \$68.2 million or \$4.90 per diluted share).

In the foreseeable future, we expect our cash needs to be funded through existing cash resources and operating cash flow. Our liquidity gives us the financial flexibility to continue to invest in our business and take advantage of opportunities in our markets, consider potential strategic acquisitions, pay shareholders dividends, and repurchase common shares under our Normal Course Issuer Bid.

### User Funds Held on Deposit

User funds held on deposit decreased 51.6% to \$10.8 million at December 31, 2008 (2007: \$22.3 million). The decrease in user funds is due primarily to the reduction in our poker business.

### Capitalization

Since inception, CryptoLogic has had neither debt nor unutilized credit facilities. At December 31, 2008, CryptoLogic had 12,728,077 common shares outstanding and 1,095,211 stock options outstanding. The 12,728,077 outstanding common shares excludes 1,090,974 (2007: 1,114,494) exchangeable shares in CryptoLogic Exchange Corporation (CEC) which are entitled to be exchanged on a one-for-one basis for common shares of the Company. Including the exchangeable shares of CEC, the outstanding common shares of the Company would be 13,819,051 (2007: 13,928,231). As of March 25, 2009 there were 12,731,979 common shares of CryptoLogic outstanding and 1,087,972 exchangeable shares in CEC outstanding.

As part of the 2007 reorganization, Canadian residents received Exchangeable Shares of CEC, an indirect subsidiary of CryptoLogic. The Exchangeable Shares are, as nearly as practicable, the economic equivalent of common shares of CryptoLogic. For accounting purposes, the acquisition is accounted for using the continuity of interest method, which recognizes CryptoLogic as the successor entity to CryptoLogic Inc. The Exchangeable Shares can be exchanged for an equivalent amount of common shares of the Company at anytime and are accounted for as a minority interest. On June 1, 2014, CryptoLogic through its subsidiaries will redeem not less than all of the then outstanding Exchangeable Shares for an amount per share equal to the redemption price. The redemption price will be satisfied through the issuance and delivery of one

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common share of CryptoLogic for each Exchangeable Share. CryptoLogic has issued a special voting share to a third party trustee, the purpose of which is to provide holders of Exchangeable Shares with the right to vote on matters to be voted on by CryptoLogic shareholders. All outstanding options of CryptoLogic Inc. as of the date of the Arrangement were fully assumed by CryptoLogic under the same terms and conditions as originally granted by CryptoLogic Inc. The Exchangeable

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Shares provide those shareholders with the same voting and dividend rights as the common shares of CryptoLogic. No additional Exchangeable Shares will be issued and all stock options will give rise to the issue of additional common shares of CryptoLogic.

From December 3, 2008 to December 2, 2009, CryptoLogic has, through its Normal Course Issuer Bid, authorization to repurchase up to 1,267,871 common shares, under which we have yet to buy back any common shares. Our buyback programs allow us to repurchase our common shares on occasions when we believe that our common share price provides an opportunity to reduce our outstanding share capital at an attractive price. Under the 2007 Normal Course Issuer Bid, we repurchased and cancelled 124,905 common shares during 2008 for a total cost of \$1.4 million.

### **Critical Accounting Estimates**

CryptoLogic's accounting policies are specified in the notes to our financial statements, in particular note 1. The accounting estimates discussed below are considered particularly important as they require judgments by management. Management has instituted policies that are intended to ensure these judgments are well controlled and consistently applied from period to period.

Each time progressive jackpot casino games are played by an end user a specified amount is added to the Jackpot. The Jackpot is won by a player on a random basis and is not predictive. Once a jackpot is won, the progressive jackpot game is reset to a predetermined amount. The Company is liable for funding the jackpot wins as well as amounts required to reset the progressive jackpot game from the pool of funds collected from participating licensees. The reset amount is provided for up to the predetermined amount, as wagering occurs.

The Company regularly performs analysis of the accumulation of jackpot funds and amounts required to address jackpot payouts. During the fourth quarter of 2009, as part of the statistical analysis of the amounts required for jackpot resets, the Company revised its estimated liability arising from the cumulative jackpot. The change in accounting estimate resulted in the reduction of the liability for jackpot accrual and a corresponding increase in revenue of \$0.8 million.

The Company may receive from time to time claims and enter into litigation arising out of the ordinary course and conduct of business including intellectual property matters. Management assesses such claims, and if considered likely to result in material exposure and where the amount of the claim is quantifiable, provisions for loss are made based on management's assessment of the likely outcome. Management does not make provisions for claims that are considered unlikely to result in a significant loss, claims for which the outcome is not determinable or claims where the amount of the loss cannot be reasonably estimated. Any settlements or awards under such claims are provided for when reasonably determinable. Adjustments will be made to the accrual for such amounts as new information is obtained or the claim settled. During the year, the Company reviewed its accounting for certain contingencies and determined \$0.8 (2008: \$1.0) million was no longer required, which increased revenue by a corresponding amount.

The Company regularly reviews its long-term assets, comprising capital assets, intangible assets and long-term investments for impairment. whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability generally requires the Company to estimate the fair value of the long-term asset, which requires the Company to make assumptions and judgments on several items including, but not limited to, the future cash flows that will be generated by these assets and the appropriate discount rate to apply to those cash flows. Measurement of any impairment loss for long-lived assets is based on the amount by which the carrying value exceeds the fair value of the asset.

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Accounting for both current and future tax requires the Company to make assumptions, judgments and estimates about current tax laws, which require certain interpretations of tax laws in several jurisdictions around the world as well as possible outcomes of current and future audits conducted by the respective tax authorities. The Company has established reserves for income taxes to address potential exposures involving tax positions that

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could be challenged by tax authorities. Although the Company believes our assumptions, judgments and estimates are reasonable, changes in tax laws or our interpretation of tax laws and the resolution of the current and any future tax audits could significantly impact the amounts provided for income taxes in its consolidated financial statements.

The Company's assumptions, judgments and estimates relative to the value of a deferred tax asset take into account predictions of the amount and category of future taxable income, such as income from operations or capital gains income. Actual operating results and the underlying amount and category of income in future years could render our current assumptions, judgments and estimates of recoverable net deferred taxes inaccurate. Any of the assumptions, judgments and estimates mentioned above could cause the Company's actual income tax obligations to differ from its estimates, thus materially impacting its financial position and results of operations.

The Company has a stock option plan where the amount of compensation expensed is determined using an option pricing model. In addition, the Company provides a long-term incentive program where the amount of the compensation expensed is determined based on estimated performance criteria and the Company's stock price. Calculations for these plans with the necessary assumptions inherently mean judgments are required by management.

### Recently issued and adopted accounting pronouncements

#### **Recently issued accounting pronouncements**

##### *International Financial Reporting Standards ( IFRS )*

In February 2008, the Accounting Standards Board ( AcSB ) confirmed that the use of IFRS will be required in 2011 for publicly accountable enterprises in Canada. In April 2008, the AcSB issued an IFRS Omnibus Exposure Draft proposing that publicly accountable enterprises be required to apply IFRS, in full and without modification, on January 1, 2011.

In June 2008 the Canadian Securities Administrators ( CSA ) issued Staff Notice 52-321, Early Adoption of IFRS which indicated that the CSA would be prepared to grant an exemption to allow Canadian financial statement issuers to adopt IFRS early on a case-by-case basis, provided that they could demonstrate that they met certain conditions.

The adoption of IFRS will require the restatement of amounts reported by us for our previous year ended, and of the opening balance sheet as at the date of adoption.

We intend to adopt IFRS for the accounting period commencing January 1, 2011 and we are continuing to assess the financial reporting impacts of the adoption of IFRS. We expect financial reporting impacts to deferred tax, intangible assets and share based payments, however, the impact on future financial position and results of operations is not reasonably determinable or estimable at this time. We do anticipate a significant increase in disclosure resulting from the adoption of IFRS and are continuing to assess the level of disclosure required.

The IFRS conversion project consists of three phases: Scoping and Diagnostics, Analysis and Development and Implementation and Review.

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Phase One: Scoping and Diagnostics, which involved project planning and staffing and identification of differences between current Canadian GAAP and IFRS, has been completed.

Phase Two: Analysis and Development, involves detailed diagnostics and evaluation of the financial impacts of various options and alternative methodologies provided for under IFRS; identification and design of operational and financial business processes; initial staff and audit committee training; analysis of IFRS 1 optional exemptions

and mandatory exceptions to the general requirement for full retrospective application upon transition to IFRS; summarization of 2011 IFRS disclosure requirements; and development of required solutions to address identified issues. Phase Two is underway, but has not yet been completed and while certain differences have been identified, we do not believe these will have any significant financial statement impact.

Phase Three: Implementation and Review will involve the execution of changes to information systems and business processes; completion of formal authorization processes to approve recommended accounting policy changes; and further training programs across our finance and other affected areas, as necessary. It will culminate in the collection of financial information necessary to compile IFRS-compliant financial statements and reconciliations; embedding of IFRS in business processes; and audit committee approval of IFRS-compliant financial statements.

***Recently adopted accounting pronouncements***

*Canadian Institute of Chartered Accountants Handbook ( Handbook ) Section 3064, Goodwill and Intangible Assets*

Section 3064, Goodwill and Intangible Assets, is effective from January 1, 2009 and converges accounting for goodwill and intangible assets under Canadian GAAP with International Financial Reporting Standards. The new standard provides more comprehensive guidance on intangible assets, particularly for internally developed intangible assets. The Company has adopted the above standard and included the required disclosures in the notes to the consolidated financial statements.

**C. RESEARCH AND DEVELOPMENT**

We make significant investments in research and development to remain competitive with technology advancements and product evolution in the global online gaming market. Research and development personnel comprised 34% of our workforce at 2009 year end (2008: 34%, 2007: 23%). Our research and development expenditures, which are accounted for as part of operating expenses, totaled \$39.9 million in 2009 (2008: \$55.6 million; 2007: \$49.4 million).

**D. TREND INFORMATION**

*Refer to the Overview at the beginning of this Item 5. Operating and Financial Review and Prospects above.*

**E. OFF-BALANCE SHEET ARRANGEMENTS**

As of March 11, 2010, the Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the Company's financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

**F. CONTRACTUAL OBLIGATIONS**

The following table summarizes our known contractual obligations as of December 31, 2009:

<i>(In thousands of U.S. dollars)</i>	<b>Total</b>	<b>Less than 1 year</b>	<b>1-3 years</b>	<b>4-5 years</b>	<b>After 5 years</b>
Facility leases, including lease termination fees	\$ 5,074	3,425	1,318	331	
Minimum royalty payments and purchase commitments	9,521	6,096	3,175	250	
Total	14,595	9,521	4,493	581	

Total cash commitments at the end of fiscal 2009 were \$14.6 million (2008: \$19.5 million). The Company has entered into lease agreements for premises expiring at various periods up to September 2013.

**G. SAFE HARBOR**

Refer to Cautionary Statement Regarding Forward-Looking Information on page 2 of this annual report.

**ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES****A. DIRECTORS AND SENIOR MANAGEMENT**

The following table and the narrative that follows set forth the name, age, residence, position, date of first election of each director and member of senior management for CryptoLogic, including the predecessor company, as at March 11, 2010.

<b>Name and Municipality of Residence</b>	<b>Age</b>	<b>Principal Occupation</b>	<b>Served as a Director<sup>(5)</sup>/ Officer Since</b>
Thomas Byrne <sup>(1)(2)(3)</sup> Dublin, Ireland	60	Director	April 13, 2007
Stephen H. Freedhoff, CA, CFP <sup>(1)(2)(6)</sup> Toronto, Ontario	74	Self-employed Chartered Accountant Director	May 1, 2003
David M.J. Gavagan <sup>(2)(4)</sup> Dublin, Ireland	58	Self-employed consultant Chairman of the Board and Director <sup>(8)</sup>	June 17, 2008
Brian Hadfield <sup>(4)</sup>	58	Self-employed Chartered Accountant Director	May 30, 2007

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Gerards Cross, England		President and CEO	
Robert H. Stikeman <sup>(3)(4)</sup>	64	Director <sup>(6)</sup>	March 7, 1996
Toronto, Ontario			
		Partner, Stikeman Keeley Spiegel Pasternack LLP (a law firm)	
Stephen B. Taylor, CA	52	Director	August 8, 2005
Dublin, Ireland			
James Wallace <sup>(1)(2)(4)</sup>	66	CFO Director	June 3, 2009
Cheshire, England			
		Self-employed chartered accountant	

- (1) Member of Audit Committee at December 31, 2009 and up to March 11, 2010..
- (2) Member of Remuneration Committee at December 31, 2009 and up to March 11, 2010.
- (3) Member of Nominating Committee at December 31, 2009 and up to March 11, 2010.
- (4) Member of Compliance and Governance Committee at December 31, 2009 and up to March 11, 2010.
- (5) Each director is elected annually to hold office until the next annual meeting of shareholders.
- (6) Mr. Freedhoff was a Director of the Company from May 1, 2003 to June 30, 2007. He rejoined as a Director of the Company on February 27, 2008.

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Biographies of each of the directors and officers set out in the above table and their respective positions held for the last five years are noted below.

**Thomas Byrne** is a Chartered Accountant and a Chartered Director. He was a partner in a global accounting firm before joining Ireland's largest brokerage firm where he was head of Corporate Finance. He set up his own corporate advisory company in 2001. Mr. Byrne is Chairman of the Board's Audit Committee. He served as Chairman of the Audit Committee of EcoSecurities Group Plc until it was privatised in late 2009. In addition to serving on the boards of SWIP 11 PLC., the Irish Takeover Panel, and the Institute of Directors in Ireland he is also a non-executive director of a number of Irish private companies.

**Stephen H. Freedhoff, CA, CFP** has been a self-employed consultant since July 1999. Prior to that, he was a partner of a Canadian national accounting firm for 30 years. Mr. Freedhoff had been a Director of the Company from May 1, 2003 to June 30, 2007, and had also served as Chairman of the Board's Audit Committee until May 31, 2007. He rejoined as a Director of the Company on February 27, 2008, and served as Chairman of the Board's Remuneration Committee until June, 2009. Mr. Freedhoff is also a non executive director at CryptoLogic Exchange Corporation.

**David M.J. Gavagan** was the co-founder and managing/senior partner of Hibernia Capital Partners, where he served in this capacity from 1996 until the fund closed in 2006. Hibernia Capital Partners was a private equity fund manager. At present, Mr. Gavagan is a self-employed Chartered Accountant and serves as a non-executive director on a number of private companies. Mr. Gavagan was appointed Chairman of the Board at the annual shareholder's meeting on June 3, 2009.

**Brian Hadfield** was appointed as the Company's President and Chief Executive Officer on February 27, 2008, and has been a Director of the Board since May 30, 2007. He had held progressively more senior positions at Unisys Limited from 1984 to 2005 and for the period 2000 to 2005 was its Managing Director.

**Robert H. Stikeman** served as Chairman of the Board from May 2003 until June 2009, and continues to serve as a Director having done so since May 30, 2002 and also has served as the Company's Secretary from 1996 until June 2009. He has been a partner for the past 20 years in Stikeman Keeley Spiegel & Pasternack LLP, a Toronto, Canada law firm he was instrumental in establishing. Mr. Stikeman holds non-executive directorships at Burnstone Ventures Inc., Isign Media Solutions, Inc. and CryptoLogic Exchange Corporation.

**Stephen B. Taylor, CA** was appointed Chief Financial Officer of the Company on August 8, 2005 and brings more than two decades of experience in financial and business management, public markets, and mergers and acquisitions. Mr. Taylor is a Chartered Accountant. Previous posts included senior financial and corporate roles at Derlan Industries, a TSX-listed aerospace company, an early-stage private software company and Vice President of Mergers and Acquisitions with Ernst & Young's corporate finance practice. Mr. Taylor spent the first 11 years of his career with Coopers & Lybrand (now PricewaterhouseCoopers) auditing multinational clients in the manufacturing, mining and financial services sectors.

**James Wallace, FCA** Mr. Wallace is a professional public company director, who currently sits on the boards of two public companies in the United Kingdom. He is currently Chairman of Scapa Group plc, the senior independent non-executive director and Audit Committee Chairman of NCC Group plc, and also a non-executive director of the Manchester Airport Group. Previously Mr. Wallace served as Chairman of Bodycote International plc until 2008, and senior independent nonexecutive director of Holidaybreak plc until 2008. Mr. Wallace also served as Chairman of Sigma Capital Group plc until 2008 and Chairman of the Audit Committee of

Sanctuary Group plc until 2007. Mr. Wallace is also a chartered accountant by profession.

No director or officer of the Company has any family relationship with any other officer or director of the Company. Members of the Board hold various non executive directorships in private companies.

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**B. COMPENSATION**

The following table presents all compensation in respect of senior management for the financial year ended December 31, 2009.

NAME AND PRINCIPAL POSITION	YEAR	SALARY US(\$) <sup>(1)</sup>	SHARE- BASED AWARDS US(\$)	OPTION- BASED AWARDS US(\$)	NON-EQUITY INCENTIVE PLAN COMPENSATION US(\$)		PENSION VALUE US(\$)	ALL OTHER COMPENSATION US(\$)	TOTAL COMPENSA-TION US(\$)
					ANNUAL INCENTIVE PLANS	LONG-TERM INCENTIVE PLANS <sup>(2)</sup>			
Brian Hadfield President and CEO and Director	2009	657,712	NIL	NIL	NIL	NIL	NIL	17,520 <sup>(3)</sup>	675,232
Stephen Taylor Chief Financial Officer	2009	254,406	NIL	NIL	NIL	161,783	17,878 <sup>(4)</sup>	308,414 <sup>(5)</sup>	742,481
Justin Thouin Vice President - Product Management and Business Development	2009	234,734	NIL	NIL	NIL	95,369	NIL	19,269 <sup>(6)</sup>	349,372
Tom McInnes Managing Director	2009	84,784	NIL	NIL	NIL	NIL	7,487	207,440 <sup>(7)</sup>	299,711
Barry Townsend	2009	NIL	NIL	NIL	NIL	NIL	NIL	269,048 <sup>(8)</sup>	269,048

<sup>(1)</sup> All amounts in this Table are expressed in US dollars. Unless otherwise indicated, where actual compensation was paid in a currency other than US dollars, the amounts in this Table are calculated based on the average effective local currency to US dollar exchange rate for fiscal year 2009.

<sup>(2)</sup> These payments were made under the Company's 2006 LTIP plan, which plan matured on December 31, 2008. The payments were made in early 2009. A portion of the value of the 2006 LTIPs was crystallized by decision of the CryptoLogic board on October 13, 2006 corresponding to the passage of the UIGEA, and were payable to employees at the completion of 3 years of employment ending December 31, 2008 (See *Long-Term Incentive Plan* below). Further grants were made under the 2007 LTIP. The 2007 LTIP plan has now matured, but no payouts were made under the plan, as the payout conditions were not achieved.

<sup>(3)</sup> This amount is made up of a car allowance.

<sup>(4)</sup> All Ireland-based employees of the Company, including Mr. Taylor, participate in a pension plan administered in accordance with Irish standards, whereby the Company makes a pre-determined contribution on behalf of Mr. Taylor.

<sup>(5)</sup> These amounts are made up of 1) amounts earned by Mr. Taylor while working away from Ireland, 2) allowances for ongoing expenses provided to Mr. Taylor associated with his relocation and the relocation of his family to Dublin, Ireland including car allowance, cost of living adjustments, housing allowances and tuition reimbursements for the educational requirements of his family and 3) a retention bonus due on each anniversary date of the date of his employment agreement with the Company up to February 14, 2010. Mr. Taylor's duties require him to spend approximately one-third of his time away from Ireland. With respect to the portion of his compensation associated with his time away from Ireland, Mr. Taylor is paid through a consulting arrangement between a wholly owned subsidiary of the Company and a corporation wholly-owned by Mr. Taylor.

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<sup>(6)</sup> This amount is made up of a car allowance and payout of unused vacation days.

<sup>(7)</sup> Mr. McInnes was a consultant prior to becoming a full time employee with the Company. These amounts represent payments to Mr. McInnes when he was engaged as a consultant.

<sup>(8)</sup> Mr. Townsend is a consultant to the Company. His primary role is to oversee the functions of our Development and Operations Groups. These amounts represents the fees from Townsend Squared Limited for the services of Mr. Townsend.

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**Incentive Plan Awards***Outstanding Share-Based Awards and Option-Based Awards*

The following table presents information relating to all share-based and option-based awards outstanding as at December 31, 2009 in respect of senior management.

NAME	OPTION-BASED AWARDS			VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS (\$)	SHARE-BASED AWARDS	
	NUMBER OF UNDERLYING UNEXERCISED OPTIONS (#)	OPTION EXERCISE PRICE (C\$) <sup>(1)</sup>	OPTION EXPIRATION DATE		NUMBER OF SHARES OR UNITS OF SHARES THAT HAVE NOT VESTED (#)	MARKET OR PAYOUT VALUE OF SHARE-BASED AWARDS THAT HAVE NOT VESTED (\$)
Brian Hadfield	100,000	\$19.00	05/15/13	NIL	NIL	NIL
Stephen Taylor	45,000	\$24.05	09/08/10	NIL	NIL	NIL
	2,500	\$24.40	02/02/11			
	25,000	\$26.80	06/27/11			
	5,000	\$29.68	01/29/12			
	25,000	\$18.56	11/13/12			
	30,000	\$19.00	05/15/13			
Justin Thouin	5,000	\$24.40	02/02/11	NIL	NIL	NIL
	20,000	\$25.08	08/04/11			
	4,000	\$29.68	01/29/12			
	25,000	\$18.56	11/13/12			
Tom McInnes	5,000	\$6.91	09/20/14	NIL	NIL	NIL
Barry Townsend	NIL	N/A	N/A			

<sup>(1)</sup> All stock option exercise prices are expressed in Canadian dollars.

*Incentive Plan Awards Value Vested or Earned During the Year*

OPTION-BASED AWARDS -  
VALUE VESTED

SHARE-BASED AWARDS -  
VALUE VESTED

NON-EQUITY INCENTIVE PLAN  
COMPENSATION - VALUE EARNED

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NAME	DURING THE YEAR (\$)	DURING THE YEAR (\$)	DURING THE YEAR (\$)
Brian Hadfield	NIL	NIL	NIL
Stephen Taylor	NIL	NIL	NIL
Justin Thouin	NIL	NIL	NIL
Tom McInnes	NIL	NIL	NIL
Barry Townsend	NIL	NIL	NIL

**Long-Term Incentive Plan**

The long-term incentive plan ( LTIP ) was adopted by the Board of Directors with effect as of January 1, 2005. The LTIP is intended to enhance the Company s ability to attract and retain high quality individuals to serve as officers and executives of the Company and to align the interests of officers and executives with those of shareholders of the Company. The LTIP provides performance-based incentives, payable in cash, Shares or a combination of both. Any payments in Shares are made through acquisitions of those Shares by the Company in the secondary market, which avoids any dilutive effect to shareholders interests. The LTIP provides for the granting of performance share units ( PSUs ) on a discretionary basis to reward participants for growth in the Company s earnings per share and share price, with vesting occurring over a 3 year period (generally referred to as

a performance cycle ). In the LTIP's inaugural year, 50% of the initial grant of PSUs was structured to vest at the end of year 2, and the remaining 50% at the end of year 3. In subsequent years, grants are generally structured to vest 100% at the end of year 3. Vesting may also be accelerated under certain circumstances, such as a change of control of the Company as defined in the LTIP, or a Participant's death. The Chief Executive Officer, the President, each Vice President, each Director or Director-level executive, each other officer of the Company and certain consultants are eligible to participate in the LTIP, on a discretionary basis. Non-employee members of the Board of Directors are not eligible participants. Generally, PSUs granted under the LTIP are not transferable. PSU grants and the financial and performance objectives required for PSUs to vest are subject to review and approval of the Remuneration Committee.

The LTIP has been designed to reward participants for growth in earnings per share and share price through overlapping three-year performance cycles. The LTIP payout is generally based upon the product of three factors: (i) The number of PSUs awarded; (ii) the share price at the end of the performance cycle; and (iii) a performance modifier that is based upon cumulative earnings per share actually achieved by the Company during the performance cycle. Generally, if cumulative targeted earnings per share are not satisfied, no payouts are made. Initial grants were made under the LTIP in 2005. PSUs granted to Mr. Salmon and Mr. Starzynski matured on December 31, 2007 and were paid out in 2008. Further grants were made under the 2006 LTIP. However, given the payout conditions associated with the 2006 LTIP, the exit by the Company from the US market in October of 2006 made it highly improbable that the 2006 LTIPs would ultimately pay anything out to holders of 2006 LTIP PSUs. As a result, the Board of Directors determined in October 2006 that the value and payment of one-third of the 2006 LTIP PSUs would be guaranteed and paid out on maturity. The 2006 LTIP matured on December 31, 2008, and holders of 2006 LTIP PSUs received payouts of the guaranteed portion of the said PSUs in early 2009. Further grants were made under the 2007 LTIP. However, payouts are not expected as it is unlikely that the target cumulative annual growth required to meet the payout conditions will be achieved. No PSUs were granted in respect of fiscal 2008 or fiscal 2009.

#### **Pension Plan Benefits**

Generally speaking, the Company does not provide pension benefits to senior management. The exceptions in this regard are: i) Mr. Taylor, in respect of whom the Company is contractually obligated to contribute an amount equal to USD \$17,931 per annum to the pension plan provided by the Company for all of its Ireland-based employees, and ii) Tom McInnes, in respect of who the Company is contractually obligated to contribute an amount equal to USD \$30,066 per annum to a pension plan. Certain other managers receive pension benefits which were not material in 2009.

#### **Termination and Change of Control Benefits**

The following is a summary of termination and change of control payments or benefits accruing to senior management. All dollar amounts have been converted to US dollars based on the average local currency exchange rate applicable during fiscal 2009.

#### **Brian Hadfield - President and CEO and Director**

The Company and Mr. Hadfield entered into an employment agreement dated March 15, 2008. Pursuant to Mr. Hadfield's employment agreement he is entitled to receive a fixed base salary. Any further review of his base salary for adjustment is to be based on an assessment of Mr. Hadfield's achievement of over-all objectives as determined by the Company. Any incremental payments that would be triggered under various termination circumstances are summarized below:

#### *Termination by the Company Other Than For Cause*

Should the Company terminate Mr. Hadfield's employment by giving notice, Mr. Hadfield will be entitled a lump sum payment made up of the following sums: (a) 12 months' base salary; and (b) 12 months' bonus, equal to the total amount of bonus received for the previous year of employment.

*Termination With Respect to a Change of Control*

(The contracts of various members of senior management contain a definition of change of control and such definitions are not necessarily identical in all cases.)

In the event Mr. Hadfield's employment is terminated in connection with a change of control of the Company, Mr. Hadfield will be entitled to a termination payment as set out above, and in addition, he will be entitled to a lump sum payment equal to 473,000.

*Voluntary Termination by Mr. Hadfield*

Mr. Hadfield must provide the Company with a minimum of ninety (90) days' written notice should he wish to voluntarily terminate his employment with the Company. In the event Mr. Hadfield voluntarily terminates his employment with the Company by providing such ninety (90) days' written notice, and the Company exercises its right to waive such notice, Mr. Hadfield will be entitled to a lump sum payment equivalent to his base salary and bonus for the balance of the notice period that remains outstanding on the date the Company exercises such waiver.

**Stephen Taylor - Chief Financial Officer**

The Company and Mr. Taylor entered into an employment agreement dated June 1, 2007. In addition, on June 1, 2007 a joint venture made up of three wholly-owned subsidiaries of the Company entered into a consulting agreement with a company wholly owned by Mr. Taylor. Pursuant to these agreements, Mr. Taylor and his company are entitled to receive gross annual remuneration at a prescribed base rate. Thereafter, his and his company's annual remuneration are subject to review by the Board of Directors of the Company on the same basis as the Board shall review the remuneration of other senior executives of the Company. Pursuant to the aforesaid agreements, Mr. Taylor and/or his company are also entitled to both discretionary bonuses and non-discretionary retention bonuses and to participate in the Company's stock option plan and LTIP. As well, the Company has agreed to make an annual pension contribution on behalf of Mr. Taylor, to the pension plan provided by the Company for all of its Ireland-based employees.

Any incremental payments that would be triggered under various termination circumstances are summarized below:

*Termination by the Company Other Than for Cause*

In the event Mr. Taylor's employment agreement is terminated by the Company other than for cause or if his employment is voluntarily terminated, under circumstances which constitute good reason (as defined in his employment agreement, which definition includes a change of control), Mr. Taylor will be entitled to the following:

**Severance or Termination Pay** - An amount equal to:

- a) Mr. Taylor's annual remuneration at the time of termination of employment; plus
- b) the greater of (i) the amount of the discretionary bonus paid to Mr. Taylor in respect of the fiscal year immediately prior to the year in which the termination takes place, or (ii) the expected amount which would be paid to Mr. Taylor as a discretionary bonus in respect of the fiscal year in which the termination takes place had Mr. Taylor remained in the employ of the Company, based on the criteria established by the senior management team bonus plan in effect at that time; plus
- c) a pro rata portion of the discretionary bonus Mr. Taylor would have received in respect of the fiscal year in which the termination arises (having regard to the portion of the fiscal year Mr. Taylor remained employed with the Company, which pro rata discretionary bonus shall be declared, calculated and paid in accordance with, and subject to the Company's senior management team bonus plan); plus
- d) A relocation allowance equal to one month's base salary, plus reimbursement of Mr. Taylor's reasonable relocation costs

**Benefits Plans** - Continued participation in the Company's benefits plans for a period of twelve (12) months following the effective date of termination.

**Stock Options** - As part and parcel of arrangements entered into at the time of Mr. Taylor's relocation to Dublin, the Company granted to Mr. Taylor certain stock options in consideration of his agreement to relocate to Dublin. Like all other options granted by the Company pursuant to its stock option plan, these options vest over time.

*Termination With Respect to a Change of Control*

In the event Mr. Taylor's employment is terminated pursuant to a change of control (as defined in his employment agreement) Mr. Taylor will be entitled to termination payments as set out above, and in addition, he will be entitled to the following:

**Stock Options** - All unvested stock options granted to Mr. Taylor will vest and be exercisable from and after the occurrence of the change of control, in the same manner, and subject to the same terms and conditions as relate to all other vested stock-options granted to Mr. Taylor.

*Termination of Consulting Agreement Other Than for Cause*

In the event the consulting agreement is terminated by the joint venture other than for cause (as defined in the consulting agreement) including without limitation, as a result of the a change of control. Mr. Taylor's consulting company will be entitled to the following:

**Severance or Termination Pay** - An amount equal to:

- a) The consulting company's annual fees at the time of termination of employment; plus
- b) the greater of (i) the amount of the discretionary bonus paid to the consulting company in respect of the fiscal year immediately prior to the year in which the termination takes place, or (ii) the expected amount which would be paid to the consulting company as a discretionary bonus in respect of the fiscal year in which the termination takes place had the consulting agreement remained in effect, based on the criteria established by the senior management team bonus plan in effect at that time; plus
- c) a pro rata portion of the discretionary bonus the consulting company would have received in respect of the fiscal year in which the termination arises (having regard to the portion of the fiscal year the consulting agreement remained in effect, which pro rata discretionary bonus shall be declared, calculated and paid in accordance with, and subject to the Company's senior management team bonus plan); plus
- d) Reimbursement for tax consulting advice relating to the relocation of Mr. Taylor, the cost of which is not to exceed 31,850.00.

*Cross Termination*

In the event that the employment agreement or the consulting agreement is terminated, the other of the agreement is contemporaneously terminated.

*Voluntary Termination by Mr. Taylor*

Mr. Taylor must provide the Company with a minimum of three (3) months notice written notice should he wish to voluntarily terminate his employment with the Company. In the event Mr. Taylor voluntarily terminates his employment with the Company on giving such three (3) months notice, and the Company exercises its right to waive such notice, Mr. Taylor will be entitled to an equivalent amount of remuneration for such period.

**Director Compensation***Director Compensation Table*

The following table presents all amounts of compensation provided to the directors for the year ended December 31, 2009

NAME <sup>(1)</sup>	FEES EARNED <sup>(2)</sup> (\$)	SHARE- BASED AWARDS (\$)	OPTION- BASED AWARDS (\$)	NON-EQUITY INCENTIVE PLAN COMPENSATION (\$)	PENSION VALUE (\$)	ALL OTHER COMPENSATION (\$)	TOTAL (\$)
Thomas Byrne	\$62,637	NIL	NIL	NIL	NIL	NIL	\$62,637
Stephen Freedhoff	\$58,120	NIL	NIL	NIL	NIL	NIL	\$58,120
David Gavagan	\$95,462	NIL	NIL	NIL	NIL	NIL	\$95,462
Robert Stikeman	\$84,620	NIL	NIL	NIL	NIL	NIL	\$84,620
James Wallace	\$36,137	NIL	NIL	NIL	NIL	NIL	\$36,137
Wai Ming Yap <sup>(3)</sup>	\$23,188	NIL	NIL	NIL	NIL	NIL	\$23,188

<sup>(1)</sup> As executive directors, Mr. Hadfield and Mr. Taylor are not separately compensated to act as directors of the Company.

<sup>(2)</sup> All amounts are in US Dollars.

<sup>(3)</sup> Wai Ming Yap resigned on 3 June 2009.

*Narrative discussion*

Director compensation consists of a retainer fee for non-executive directors and additional fees in connection with service as Board Chairman or committee chairs. For the most recently completed financial year, director fees were set at GBP 35,000 per annum (\$54,589 per annum, based on the average effective GBP to US dollar exchange rate for fiscal year 2009), with an additional GBP 5,000 (\$7,798, based on the average effective GBP to US dollar exchange rate for fiscal year 2009) payable in connection with serving as a committee chair, and an additional GBP 45,000 (\$70,186 based on the average effective GBP to US dollar exchange rate for fiscal year 2009) payable in connection with serving as Chairman of the Board of Directors of the Company.

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*Outstanding Share-Based Awards and Option-Based Awards*

The following table presents information relating to all share-based and option-based awards outstanding as at December 31, 2009 in respect of each director.

NAME	OPTION-BASED AWARDS				SHARE-BASED AWARDS	
	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS (#)	OPTION EXERCISE PRICE (C\$)	OPTION EXPIRATION DATE	VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS (\$)	NUMBER OF SHARES OR UNITS OF SHARES THAT HAVE NOT VESTED (#)	MARKET OR PAYOUT VALUE OF SHARE-BASED AWARDS THAT HAVE NOT VESTED (\$)
Stephen Freedhoff	3,333	\$21.39	09/02/10	NIL	NIL	NIL
	10,000	\$23.56	12/14/11	NIL	NIL	NIL
Robert Stikeman	12,000	\$21.39	09/02/10	NIL	NIL	NIL
	45,000	\$23.56	12/14/11	NIL	NIL	NIL

*Incentive Plan Awards Value Vested or Earned During the Year*

NAME	OPTION-BASED AWARDS - VALUE VESTED DURING THE YEAR (\$)	SHARE-BASED AWARDS - VALUE VESTED DURING THE YEAR (\$)	NON-EQUITY INCENTIVE PLAN COMPENSATION -- VALUE EARNED DURING THE YEAR (\$)
Stephen Freedhoff	NIL	NIL	NIL
Robert Stikeman	NIL	NIL	NIL

**C. BOARD PRACTICES**

All Directors are elected annually by the Company's shareholders and hold office until the next Annual Meeting of Shareholders. The Directors' service contracts do not provide for benefits upon termination of service.

The Board of Directors is responsible for the general supervision of the management of the business. The Board will meet regularly to review the business operations, corporate governance and financial results of the Company.

The Board will discharge its responsibilities directly or through its committees, which consist of the Audit Committee, the Remuneration Committee, the Compliance and Governance Committee and the Nominating Committee. Copies of the Terms of Reference for each committee are available on our website at [www.cryptologic.com](http://www.cryptologic.com).

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For information concerning the period during which the current directors have served as director of the Company, see Item 6.A. Directors and Senior Management .

### Audit Committee

The members of the Audit Committee are Thomas Byrne, Stephen Freedhoff and James Wallace. Mr. Byrne serves as Chairman of the Audit Committee. Each member is independent as that term is defined by the NASDAQ listing standards applicable to the Company. The Audit Committee normally meets a minimum of four times per year.

The overall purpose of the Audit Committee is to monitor the Company's system of internal financial controls and procedures, to evaluate and report on the integrity of the financial statements of the Company, to enhance the independence of the Company's external auditors and to oversee the financial reporting process of the Company.

Remuneration Committee

The members of the Remuneration Committee are James Wallace, David Gavagan, Thomas Byrne and Stephen Freedhoff, all of whom are independent directors. Mr. Wallace serves as the Chairman of the Remuneration Committee. The Remuneration Committee normally meets a minimum of two times per year.

The duties of the Remuneration Committee include recommending to the Board appropriate human resource and compensation policies for the Company. The Remuneration Committee has responsibility for reviewing compensation for the directors and officers. The committee periodically reviews the adequacy and form of the compensation of the directors of the Company with a view to ensuring that such compensation realistically reflects the responsibilities and risks of being a director.

Compliance and Governance Committee

The members of the Compliance and Governance Committee are David Gavagan, Thomas Byrne, James Wallace and Robert Stikeman. Mr. Gavagan serves as Chairman of the Compliance and Governance Committee. The Compliance and Governance Committee normally meets not less than once per year.

The Compliance and Governance Committee is responsible for reviewing the Company's corporate governance (committees, mandates and composition) on an annual basis to ensure: (i) adherence to best practices based on evolving industry standards; and (ii) legal compliance with all applicable statutes and regulations pertaining to, among other things, financial reporting, internal controls, disclosure of a non-financial nature, as well as the evolution of fiduciary standards, and prescribed by statute, regulation and as it evolves in common law.

The Compliance and Governance Committee also reviews the Company's compliance practice relating to the license and certification of its subsidiary's gaming software to the Internet gaming industry, reviewing all probity reports requested respecting its subsidiaries' licensees, and assessing global legislative developments as they may affect the Company's business around the world.

Nominating Committee

The Board of Directors considers its size each year when it considers the number of Director nominees to recommend to the shareholders for election at the annual meeting of shareholders, taking into account the number required to carry out the Board's duties effectively and to maintain a diversity of views and experience.

The members of the Nominating Committee are David Gavagan, Thomas Byrne, and Robert Stikeman. Mr. Gavagan serves as Chairman of the Nominating Committee.

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The Nominating Committee normally meets when appropriate, but at least once per year. The Nominating Committee reviews the skills of the prospective directors, identifies any deficiencies and directs interviewing of suitable candidates. In order to encourage an independent nominating process, once a candidate is identified, such candidate meets with the Directors on an individual basis and as a group to discuss the Company's business and regulatory activities. The Directors then receive a recommendation from the Nominating Committee on any candidate, who must be approved by the Board as a whole.

**D. EMPLOYEES**

The following table sets forth information detailing the total number of employees at the years ended December 31, 2009, 2008 and 2007, which excluded an average of 19 consultants or independent contractors during the most recent financial year.

	<b>2009</b>	<b>% Total</b>	<b>2008</b>	<b>% Total</b>	<b>2007</b>	<b>% Total</b>
Total number of employees	211	100%	276	100%	300	100%
By country						
Canada	94	45%	151	55%	181	61%
United Kingdom	43	20%	35	13%	33	11%
Cyprus	41	19%	65	23%	76	25%
Ireland	25	12%	17	6%	3	1%
Other	8	4%	8	3%	7	2%

**E. SHARE OWNERSHIP**

The following table sets forth, as of March 30, 2010, the number of the Company's Common Shares (including Exchangeable Shares) beneficially owned by the then serving senior management and Directors of the Company, individually, and as a group, and the percentage of ownership of the outstanding Common Shares (including Exchangeable Shares) represented by such shares.

The Common Share (including Exchangeable Shares) held by senior management and Directors listed below have voting rights no different than the voting rights associated with Common Shares generally.

<b>Name of Beneficial Owner</b>	<b>Common Shares Held</b>	
		<b>Percent of Class</b>
Thomas Byrne	8,000	*
Stephen H. Freedhoff	13,333 <sup>(1)</sup>	*
David Gavagan	3,000	*
Brian Hadfield	107,350 <sup>(1)</sup>	*
Thomas McInnes	5,000 <sup>(1)</sup>	*
Robert Stikeman	62,000 <sup>(1)</sup>	*
Stephen B. Taylor	141,200 <sup>(1)</sup>	1.0
Justin Thouin	54,000 <sup>(1)</sup>	*
Barry Townsend		*
Senior Management and Directors of the Company as a group (7 persons)	393,883 <sup>(1)</sup>	2.9

<sup>(1)</sup> Includes the following options to purchase Common Shares:

\* Less than 1%.

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Name	Number of Options (#)	Exercise Price (C\$)	Date of Expiration
Stephen H. Freedhoff	3,333	21.39	September 2, 2010
Brian Hadfield	10,000	23.56	December 14, 2011
Tom McInnes	100,000	19.00	May 15, 2013
Robert Stikeman	5,000	6.91	September 20, 2014
	12,000	21.39	September 2, 2010
Stephen B. Taylor	45,000	23.56	December 14, 2011
	45,000	24.05	August 9, 2010
	2,500	24.40	February 2, 2011
	25,000	26.80	June 27, 2011
	5,000	29.68	January 29, 2012
	25,000	18.56	November 13, 2012
	30,000	19.00	May 15, 2013
Justin Thouin	5,000	24.40	February 2, 2011
	20,000	25.08	August 4, 2011
	4,000	29.68	January 29, 2012
	25,000	18.56	November 13, 2012

**Stock Option Plan**

The Company maintains a Stock Option Plan for its directors, officers and employees. The principal features of the Stock Option Plan are as follows:

The Stock Option Plan authorizes the issuance of 3,900,000 options. As of December 31, 2009, there were 916,691 options are available for issuance under the Stock Option Plan.

Options have a term of five years or less and will be subject to earlier termination in certain circumstances. An option will only become exercisable after the following vesting periods:

- o one-third of the options granted to Directors will vest at the date of grant, one additional third one year thereafter, and the remaining third one year after that;
- o unless otherwise permitted by the Remuneration Committee, all other options granted will vest at a rate of one-quarter of the total amount granted per year, the first vesting date to follow one year after the date of grant. Vesting dates will follow annually on the anniversary date of the original grant, provided that in the event of a public takeover bid all options will immediately vest.

Any option granted under the Option Plan, to the extent that such option has not been validly exercised, will terminate on the earlier of the following dates: (i) the date of expiration specified in the option agreement; (ii) 30 days after the date of the termination or expiration of the optionee's employment, directorship or service agreement other than by cause and other than by retirement, permanent disability or death; (iii) six (6) months after the date of the optionee's death; and (iv) three (3) months after termination of

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the optionee's employment by permanent disability or retirement under any retirement plan of the Company.  
No one person may receive or hold options entitling the purchase of 5% or more the outstanding Common Shares of the Company.

The exercise price is fixed by the directors but is not less than the market value of the Common Shares at the date of the grant (the closing price on the day of the grant or the average between highest and lowest prices on such day).  
Stock options are not assignable by the holder.

The CEO may issue up to 5,000 options to non-executive staff members without approval from the remuneration committee. However the CEO must report any issuances immediately.

No financial assistance will be provided by the Company to option holders in connection with the exercise of stock options granted under the Stock Option Plan.

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The Stock Option Plan is administered by the Board of Directors on the advice of the Remuneration Committee.

Amendments to the Stock Option Plan require the approval of the directors and those shareholders not otherwise eligible to receive a benefit under the plan.

The following table sets forth the number of Common Shares authorized for issuance under the Stock Option Plan as at December 31, 2009.

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Stock Option Plan	563,521	C\$21.89	916,691

### **Employee Share Purchase Plan**

In 2005, the Company established an Employee Share Purchase Plan to provide employees with an opportunity to purchase Shares, further participants' alignment with the interests of shareholders and allow them to participate in the growth of the Company. Participation is limited to eligible employees and independent consultants of the Company and its subsidiaries. Employees become eligible after six months of employment with the Company. There are four (4) offering periods (each, an Offering Period) per year (once a quarter), as determined by the Board of Directors. Shares will be purchased, through an agent, at market value on the open market of the Toronto Stock Exchange. Employees may elect to purchase shares through a cash transaction at the beginning of the Offering Period, or through payroll deductions over a 12 month period. Employees can contribute up to 10% of their salary (excluding bonuses). The Company will match 50% of the employee's contribution, subject to a C\$2,500 annual limit. Shares purchased with Company match funds will have a 12 month hold period (from the date of purchase).

In 2009, 19,651 Common Shares were purchased at an average price of US\$7.73. As at December 31, 2009 there were 16,719 Shares held under the Employee Share Purchase Plan.

## **ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS**

### **A. MAJOR SHAREHOLDERS**

As at March 11, 2010, there were 12,798,120 Common Shares and 1,020,931 Exchangeable Shares. Including Exchangeable Shares, the Common Shares outstanding would be 13,819,051. The holders of Exchangeable Shares are entitled to one vote per Exchangeable Share. CryptoLogic Limited has issued a special voting share to a third party trustee, the purpose of which is to provide holders of Exchangeable Shares with the right to vote on CryptoLogic matters. For the purposes of the table below, the number of Common Shares and Exchangeable Shares are added together to determine the percentage of votes held.

The following table sets forth information regarding beneficial ownership of our Common Shares as of March 11, 2010 by each person or organization that is known to us to own beneficially or exercise control or direction over shares carrying more than 5% of our outstanding Common Shares.



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Name and Location of Beneficial Owner	Number of Common Shares	Percent of Common Shares Outstanding (excluding Exchangeable Shares)	Percent of Common Shares Outstanding (including Exchangeable Shares) <sup>(4)</sup>
Royce & Associates, LLC New York, U.S.A.	1,233,875 <sup>(1)</sup>	9.64%	8.92%
Renaissance Technologies Corp. New York, U.S.A.	879,437 <sup>(2)</sup>	6.87%	6.36%
Austin W. Marx and David M. Greenhouse New York, U.S.A.	1,396,288 <sup>(3)</sup>	10.91%	10.10%

<sup>(1)</sup> Based upon information reported by Royce & Associates, LLC in a Schedule 13G/A filed with the SEC on January 30, 2010 with respect to its beneficial ownership as of December 31, 2009.

<sup>(2)</sup> Based upon information reported by Renaissance Technologies Corp in a Schedule 13G/A filed with the SEC on February 13, 2010 with respect to its beneficial ownership as of December 31, 2009.

<sup>(3)</sup> Based upon information reported by Austin W. Marx and David M. Greenhouse in a Schedule 13G filed with the SEC on March 2, 2010 with respect to their beneficial ownership as of December 31, 2009. Messrs. Marx and Greenhouse are the controlling principals of AWM Investment Company, Inc. ( AWM ), the general partner of and investment adviser to Special Situations Cayman Fund, L.P ( Cayman ). AWM also is the general partner of MGP Advisers Limited Partnership ( MGP ), which is the general partner of and investment advisor to Special Situations Fund III QP, L.P. ( SSFQP ). Messrs. Marx and Greenhouse are also members of SST Advisors, L.L.C., the general partner of Special Situations Technology Fund, L.P. ( Tech ) and Special Situations Technology Fund II, L.P. ( Tech II ). AWM serves as the investment adviser to SSFQP, Tech and Tech II. Of the 1,396,288 shares reported in the Schedule 13G, 305,816 shares are owned by Cayman, 928,897 shares are owned by SSFQP , 22,084 shares are owned by Tech and 139,491 shares are owned by Tech II.

<sup>(4)</sup> Based upon 13,819,051 shares outstanding (including Exchangeable Shares) as of March 11, 2010 and presuming the listed beneficial owners' position remained unchanged.

The Common Shares held by the major shareholders listed above have voting rights no different than the voting rights associated with Common Shares generally.

As at March 11, 2010, we believe there were seven record holders of our Common Shares in the U.S., holding 99.5% of the outstanding Common Shares (excluding Exchangeable Shares). However, we believe the number of beneficial shareholders is much higher, as the bulk of the shares held by these seven registered holders are held in trust for others. To our knowledge, the Company's Exchangeable Shares are only held by Canadian residents.

As far as is known to the Company, CryptoLogic is not directly or indirectly owned or controlled by another corporation, by another foreign government or by any other natural or legal person severally or jointly.

### **B. RELATED PARTY TRANSACTIONS**

In the normal course of operations, the Company engages the services of Stikeman Keeley Spiegel Pasternack LLP, a law firm in which Robert Stikeman (Chairman of the Board of Directors) is a partner. Fees paid to this firm were \$0.06 million in 2009 (2008: \$0.4 million). In fiscal 2009, the Company determined that Stikeman Keeley Spiegel Pasternack LLP would no longer act as primary outside counsel and its services are being transitioned to another law firm.

The Company incurred \$0.03 million (2008: \$0.01 million) in fees to Stamford Law Corporation, a law firm in which Wai Ming Yap (a former member of the Board of Directors) is a partner.

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**ITEM 8. FINANCIAL INFORMATION**

**A. CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION**

Refer to Item 17. Financial Statements for a list of financial statements filed with this annual report.

Legal Proceedings

As at March 11, 2010 the Company and its subsidiaries are not involved nor have they been involved in any legal or arbitration proceedings (including any such proceedings which are pending or threatened, of which the Company or its subsidiaries are aware) which may have, or have had in the past 12 months a significant effect on our financial position or profitability, with the exception of the following:

On March 30, 2010, the Company delivered to Marvel a Statement of Claim regarding an alleged breach by Marvel of certain provisions of its agreement with the Company relating to the licensing of Marvel comic book characters to CryptoLogic. Any proceeding flowing from the said Statement of Claim must proceed by way of arbitration in the City of New York and under New York law, as per the contract with Marvel.

Given the nature of the business environment in which we operate and the relative strength of our financial position, third parties have threatened to issue legal proceedings against the Company based on alleged infringement of patents, trademark, copyright and/or other intellectual property rights. None of these threats has as yet resulted in legal proceedings, although there can be no assurance that the assertion of such claims will not result in litigation or that the Company would prevail in any such litigation. An adverse determination in litigation proceedings could subject the Company to significant liabilities to third parties. Although patent and intellectual property disputes are often settled through licensing or similar arrangements, the costs associated with such arrangements may be substantial and could include ongoing royalties. Furthermore, the necessary licenses may not be available to the Company on satisfactory terms, if at all.

The Company closely monitors the progress of all threatened litigation and, where the Board of Directors consider it appropriate, makes the appropriate provisions and reserves in its financial statements for litigation contingencies that are likely to result in material exposure and the amount is quantifiable.

Dividend Policy

On September 10, 2003, the Board of Directors declared the Company's first quarterly dividend of \$0.03 per Common Share (annual rate of \$0.12), paid on November 24, 2003. On November 4, 2004, the Board approved an increase in our quarterly dividend to \$0.05 per Common Share (annual rate of \$0.20). On November 1, 2005, the quarterly rate was increased to \$0.07 per Common Share (annual rate of \$0.28). On May 9, 2006, the Company announced a subsequent increase to \$0.12 per Common Share per quarter (annual rate of \$0.48). On February 14, 2007, a quarterly dividend of \$0.12 per Common Share was announced, the same rate as the prior four quarters and for the remaining quarters of 2007. On November 12, 2008, we announced the Board's decision to decrease the dividend to \$0.03 per common share (annual rate of \$0.12), commencing with the quarterly dividend paid on December 15, 2008. On March 13, 2009, a dividend of \$0.03 per common share was

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announced. The holders of Exchangeable Shares and Common Shares participate equally in voting and dividends. On November 13, 2009, we announced the Board's decision to decrease the dividend to \$0.01 per common share (annual rate of \$0.04), commencing with the quarterly dividend paid on December 15, 2009. CryptoLogic did not declare a dividend for the fourth quarter 2009 and does not expect to declare any further dividends for the foreseeable future. However the decision as to whether or not to declare a quarterly dividend in the future will be duly considered by the Board, having regard to the Company's financial results.

**B. SIGNIFICANT CHANGES**

There have been no significant changes to the Company's financial information since December 31, 2009.

**ITEM 9. THE OFFER AND LISTING**

The following table sets forth, for the periods indicated, the range of the high and low prices of our Common Shares as reported by the Toronto Stock Exchange (symbol: CRY), NASDAQ Global Select Market (symbol: CRYP) and the Main Market of the London Stock Exchange (symbol: CRP):

	<b>Toronto Stock Exchange</b>		<b>NASDAQ</b>		<b>London Stock Exchange</b>	
	<b>(C\$)</b>		<b>(US\$)</b>		<b>(British pence)</b>	
	<b>High</b>	<b>Low</b>	<b>High</b>	<b>Low</b>	<b>High</b>	<b>Low</b>
Fiscal Year Ended December 31, 2009	10.19	3.01	8.60	2.35	547.50	185.00
Fiscal Year Ended December 31, 2008	22.20	2.06	21.77	2.08	1,120.00	150.00
Fiscal Year Ended December 31, 2007	34.81	17.00	31.20	17.26	1,520.00	893.50
Fiscal Year Ended December 31, 2006	33.09	17.06	29.20	15.24	1,625.00	872.50
Fiscal Year Ended December 31, 2005	45.88	17.60	36.81	14.84	1,960.00	852.50
Fiscal Year Ended December 31, 2009						
First Quarter	7.40	3.03	6.01	2.35	403.75	205.00
Second Quarter	10.19	5.68	8.60	4.59	547.50	337.50
Third Quarter	8.05	6.32	7.44	5.87	443.00	370.00
Fourth Quarter	6.61	3.01	6.42	2.90	400.00	185.00
Fiscal Year Ended December 31, 2008						
First Quarter	18.00	14.10	17.82	14.66	909.00	751.00
Second Quarter	22.20	14.30	21.77	14.29	1,120.00	720.00
Third Quarter	14.80	5.13	13.93	5.17	697.50	322.75
Fourth Quarter	6.49	2.06	5.4	2.08	358.50	150.00
September 2009	7.64	6.32	6.98	5.90	443.00	370.00
October 2009	6.61	4.11	6.42	3.80	400.00	265.00
November 2009	4.43	3.30	4.13	3.22	270.00	200.00
December 2009	3.85	3.01	3.66	2.90	230.00	185.00
January 2010	3.87	3.17	3.74	2.97	215.00	195.00
February 2010	3.51	3.18	3.36	2.97	200.00	190.00

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The following table sets forth, for the periods indicated, the range of the high and low prices of our Exchangeable Shares as reported by the Toronto Stock Exchange (symbol: CXY):

	Toronto Stock Exchange <sup>(1)</sup>	
	(C\$)	
	High	Low
Fiscal Year Ended December 31, 2009	10.00	2.76
Fiscal Year Ended December 31, 2009		
First Quarter	7.40	2.76
Second Quarter	10.00	5.50
Third Quarter	7.90	6.25
Fourth Quarter	6.55	3.00
Fiscal Year Ended December 31, 2008	22.90	2.75
Fiscal Year Ended December 31, 2008		
First Quarter	20.50	15.50
Second Quarter	22.90	16.10
Third Quarter	15.50	6.50
Fourth Quarter	6.54	2.75
September 2009	7.80	6.25
October 2009	6.55	4.12
November 2009	4.25	3.20
December 2009	3.70	3.00
January 2010	3.71	3.23
February 2010	3.40	3.06

### **ITEM 10. ADDITIONAL INFORMATION**

#### **A. SHARE CAPITAL**

Not applicable.

#### **B. MEMORANDUM AND ARTICLES OF ASSOCIATION**

The following information is a summary and is subject to the detailed provisions of our Memorandum of Association (the "Memorandum") and Articles of Association (the "Articles"). A copy of the Company's Memorandum and Articles are incorporated herein by reference to Exhibits 1.1 and 1.2 to this annual report.

##### **Objects and Purpose**

On April 13, 2007, CryptoLogic Limited was incorporated under the laws of Guernsey with registered number 46770, but with its corporate headquarters in Dublin, Ireland where it operates and is resident for tax purposes. The Company's registered office is located at 1 Le Marchant Street, St. Peter Port, Guernsey, Channel Islands, GY1 4HP. The Company's head office is located at Marine House, Clanwilliam Place, Dublin 2, Ireland.

The Memorandum provides that the Company's objects are, *inter alia*, to carry on business as a general commercial company. The objects of the Company are set out in full in clause 3 of the Memorandum.

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Directors and Powers

The Company's Articles specify a maximum number of ten directors. A director shall continue in office until his or her successor is elected at the next shareholders' meeting. Incumbent directors, if qualified, shall be eligible for re-election.

Subject to the Articles or any unanimous shareholders agreement, the board may fix the remuneration of the directors. Such remuneration shall be in addition to any salary or professional fees payable to a director who services the Company in any other capacity. In addition, directors shall be paid sums in respect of their out-of-pocket expenses incurred in attending board, committee or shareholders' meetings or otherwise in respect of the performance by them of their duties as the board may from time to time determine.

Every director of the Company who is a party to a material contract or proposed material contract with the Company, or is a director or has a material interest in any corporation which is party to a material contract or proposed material contract with the Company shall disclose to the Board the nature and extent of his interest. A director may vote in respect of any contract or arrangement in which he has a material interest.

Directors of the Company do not have to retire under an age limit requirement and are not required to own shares of the company in order to serve as directors. Directors' borrowing powers are not generally restricted where the borrowing is in the Company's best interests.

Rights and Privileges of Common Shares

Our Articles provide that our authorized share capital is an unlimited number of Common Shares at no par value and one special voting share. Every shareholder is entitled to one vote for each share held on all matters submitted to shareholder meetings, including the election and removal of directors. The Board may from time to time declare, and the Company may pay a dividend to shareholders on its outstanding shares according to their respective rights in the Company. All dividends unclaimed for a period of six years after having been declared shall be forfeited and shall revert to the Company. All questions proposed for the consideration of the shareholders at a meeting, including all elections for directors, shall be decided by majority vote, except as otherwise required by the Act. Holders of Exchangeable Shares are entitled to vote through the special voting share, a voting trust arrangement established under the Arrangement as described on page 1 of this annual report.

A special resolution (requiring a three-fourth majority) is required to amend our Articles in such circumstances as to change any maximum number of shares that we are authorized to issue, to create new classes of shares, to change the designation of all or any of our shares and add, change or remove any rights privileges, restrictions and conditions including rights to accrued dividends, in respect of all or any of our shares, whether issued or unissued.

The conditions governing the manner in which annual general meetings and special meetings of shareholders are convoked are contained in Articles 15-19:

*Annual Shareholders' Meeting*

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The annual meeting of shareholders of the Company shall be held at such time and on such day each year as the board may from time to time determine, for the purpose of receiving the reports and statements to be laid before the annual meeting, electing directors, appointing auditors, and for the transaction of such other business as may properly be brought before the meeting.

### *Special Shareholders Meeting*

The board may at any time call a special meeting of shareholders for the transaction of any business, which may properly be brought before such meeting of shareholders. The board also shall call a special meeting upon the

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valid and appropriate requisition in writing of one or more shareholders representing not less than 10% of the shares in issue.

All business transacted at an annual meeting of shareholders, except consideration of financial statements, auditor's report, election of directors and reappointment of the incumbent auditor, is deemed to be special business.

### *Quorum*

The holders of not less than 25% of the shares entitled to vote at a meeting of shareholders present in person or by proxy constitutes a quorum for the transaction of business at any meeting of shareholders.

### *Votes of Shareholders*

At any meeting of shareholders, unless the Articles otherwise provide, each share of the Company entitles the holder thereof to one vote at a meeting of shareholders, and the special voting share authorizes additional votes on the basis of one additional vote for each Exchangeable Share held other than by the Company or its affiliates.

### *Proxies*

Every shareholder entitled to vote at a meeting of shareholders may by means of a proxy appoint a proxy holder or one or more alternate proxy holders who are not required to be shareholders to attend and act at the meeting in the manner and to the extent authorized by the proxy and with the authority conferred by the proxy.

A proxy shall be in writing and executed by the shareholder or by his attorney authorized in writing.

### *Notice of Meeting*

Notice of the time and place of each meeting of shareholders shall be sent not less than 10 days and not more than 50 days before the date of the meeting to the auditor of the Company (if any), to each director, and to each person whose name appears on the records of the Company at the close of business on the day next preceding the giving of the notice as a shareholder entitled to vote at the meeting.

There are no limitations on the rights to own our securities, including the rights of non-resident or foreign shareholders to hold or exercise voting rights on our securities imposed by foreign law or under the Company's Articles.

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There are no provisions in the Company's Articles that would have an effect of delaying, deferring, or preventing a change in control of the Company.

There are no provisions in the Company's Articles governing an ownership threshold above which shareholder ownership must be disclosed.

### **C. MATERIAL CONTRACTS**

In May 2008, we acquired an 11.1% interest in Jingle Prize Inc., a supplier of online mahjong games, for \$1 million. In exchange for the cash consideration, we received preference shares, which rank pari passu with the common shares of Jingle with respect to all dividends and voting rights. The terms of this agreement require us to make additional investments in Jingle if certain performance criteria are met. In December 2008, the first performance criteria were met resulting in an additional investment of \$0.7 million, increasing our equity ownership in Jingle to 18.9%.

#### **D. EXCHANGE CONTROLS**

Not applicable.

#### **E. TAXATION**

The following is a general discussion of certain possible U.S. federal income tax consequences, under current law, generally applicable to a U.S. Holder of shares of the Company. This discussion is of a general nature only and does not take into account the particular facts and circumstances, with respect to U.S. federal income tax issues, of any particular U.S. Holder. In addition, this discussion does not cover any state, local or foreign tax consequences.

*This discussion is for general information only and it is not intended to be, nor should it be construed to be, legal or tax advice to any U.S. Holder or prospective U.S. Holder of shares of the Company, and no opinion or representation with respect to the U.S. federal income tax consequences to any such U.S. Holder or prospective U.S. Holder is made. Accordingly, U.S. Holders and prospective U.S. Holders of shares of the Company should consult their own financial advisor, legal counsel or accountant regarding the U.S. federal, state, local and foreign tax consequences of purchasing, owning and disposing of shares of the Company.*

#### **U.S. FEDERAL INCOME TAX CONSIDERATIONS**

##### **Ownership of CryptoLogic Shares**

The following is a summary of certain material U.S. federal income tax consequences to a U.S. Holder (as defined below) of the acquisition, ownership and disposition of CryptoLogic shares.

##### **Scope of this Summary**

##### **Authorities**

This summary is based on the Internal Revenue Code of 1986, as amended (the Code), Treasury Regulations (whether final, temporary, or proposed), published rulings of the Internal Revenue Service (the IRS), published administrative positions of the IRS, the Convention Between the Government of the United States and the Government of Ireland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains, signed at Dublin on July 28, 1997 as amended (the Convention), and U.S. court decisions that are applicable and, in each case, as in effect and available, as of the date of this annual report. Any of the authorities on which this summary is based could be changed in a material and adverse manner at any time, and any such change could be applied on a retroactive basis. This summary does not discuss the potential effects, whether adverse or beneficial, of any proposed legislation that, if enacted, could be applied on a retroactive basis.

U.S. Holders

For purposes of this summary, a U.S. Holder is a beneficial owner of CryptoLogic shares that, for U.S. federal income tax purposes, is (a) an individual who is a citizen or resident of the U.S., (b) a corporation, or any other entity classified as a corporation for U.S. federal income tax purposes, that is created or organized in or under the laws of the U.S. or any state in the U.S., including the District of Columbia, (c) an estate if the income of such estate is subject to U.S. federal income tax regardless of the source of such income, or (d) a trust if (i) such trust has validly elected to be treated as a U.S. person for U.S. federal income tax purposes or (ii) a U.S. court is able to exercise primary supervision over the administration of such trust and one or more U.S. persons have the authority to control all substantial decisions of such trust.

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### Non-U.S. Holders

For purposes of this summary, a non-U.S. Holder is a beneficial owner of CryptoLogic shares other than a U.S. Holder. This summary does not address the U.S. federal income tax consequences of the acquisition, ownership, and disposition of CryptoLogic shares to non-U.S. Holders. Accordingly, a non-U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the U.S. federal income, U.S. state and local, and foreign tax consequences (including the potential application of and operation of any tax treaties) of the acquisition, ownership, and disposition of CryptoLogic shares.

### U.S. Holders Subject to Special U.S. Federal Income Tax Rules Not Addressed

This summary does not address the U.S. federal income tax consequences of the acquisition, ownership, and disposition of CryptoLogic shares to U.S. Holders that are subject to special provisions under the Code, including the following U.S. Holders: (a) U.S. Holders that are tax-exempt organizations, qualified retirement plans, individual retirement accounts, or other tax-deferred accounts; (b) U.S. Holders that are financial institutions, insurance companies, real estate investment trusts, or regulated investment companies; (c) U.S. Holders that are dealers in securities or currencies or U.S. Holders that are traders in securities that elect to apply a mark-to-market accounting method; (d) U.S. Holders that have a functional currency other than the U.S. dollar; (e) U.S. Holders that are liable for the alternative minimum tax under the Code; (f) U.S. Holders that own CryptoLogic Shares as part of a straddle, hedging transaction, conversion transaction, constructive sale, or other arrangement involving more than one position; (g) U.S. Holders that acquired CryptoLogic shares in connection with the exercise of employee stock options or otherwise as compensation for services; (h) U.S. Holders that hold CryptoLogic shares other than as a capital asset within the meaning of Section 1221 of the Code, (i) U.S. Holders that own (directly, indirectly, or by a attribution) 10% or more of the total combined voting power of the outstanding shares of CryptoLogic or (j) U.S. Holders that are expatriates or former long-term residents of the United States. U.S. Holders that are subject to special provisions under the Code, including U.S. Holders described immediately above, should consult their own financial advisor, legal counsel or accountant regarding the U.S. federal income, U.S. state and local, and foreign tax consequences of the acquisition, ownership, and disposition of CryptoLogic shares.

If an entity that is classified as a partnership (or pass-through entity) for U.S. federal income tax purposes holds CryptoLogic shares, the U.S. federal income tax consequences to such partnership (or pass-through entity) and the partners of such partnership (or owners of such pass-through entity) generally will depend on the activities of the partnership (or pass-through entity) and the status of such partners (or owners). Partners of entities that are classified as partnerships (or owners of pass-through entities) for U.S. federal income tax purposes should consult their own financial advisor, legal counsel or accountant regarding the U.S. federal income tax consequences of the acquisition, ownership, and disposition of CryptoLogic shares.

### Tax Consequences Other than U.S. Federal Income Tax Consequences Not Addressed

This summary does not address the U.S. state and local, U.S. federal estate and gift, or foreign tax consequences to U.S. Holders of the acquisition, ownership, and disposition of CryptoLogic shares. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the U.S. state and local, U.S. federal estate and gift, and foreign tax consequences of the acquisition, ownership, and disposition of CryptoLogic shares.

### Distributions on CryptoLogic Shares. Tax Consequences of Distributions in General

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Subject to the PFIC rules discussed below, a U.S. Holder that receives a distribution, including a constructive distribution, with respect to the CryptoLogic shares will be required to include the amount of such distribution in gross income as a dividend (without reduction for any Irish income tax withheld from such distribution) to the extent of the current or accumulated earnings and profits of CryptoLogic, as computed for U.S. federal income tax purposes. To the extent that a distribution exceeds the current and accumulated earnings and profits of CryptoLogic, such distribution will be treated first as a tax-free return of capital to the extent of a

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U.S. Holder's adjusted tax basis in the CryptoLogic shares and thereafter as gain from the sale or exchange of such CryptoLogic shares. (See Disposition of CryptoLogic Shares below). Dividends received on the CryptoLogic shares generally will not be eligible for the dividends received deductions.

### Reduced Tax Rates for Certain Dividends

For taxable years beginning before January 1, 2011, a dividend paid by CryptoLogic generally will be taxed at the preferential tax rates applicable to long-term capital gains if (a) CryptoLogic is a qualified foreign corporation (as defined below); (b) the U.S. Holder receiving such dividend is an individual, estate, or trust; and (c) such dividend is paid on CryptoLogic shares that have been held by such U.S. Holder for at least 61 days during the one hundred and twenty-one (121) day period beginning sixty (60) days before the ex-dividend date.

CryptoLogic generally will be a qualified foreign corporation under Section 1(h)(11) of the U.S. Code (a QFC) if CryptoLogic is eligible for the benefits of the U.S.-Ireland Income Tax Treaty or, if not, the CryptoLogic shares are readily tradable on an established securities market in the U.S. CryptoLogic believes that it was a QFC for the previous taxable year and expect that it will be a QFC for the current taxable year. However, even if CryptoLogic satisfies one or more of the QFC requirements, CryptoLogic will not be treated as a QFC if CryptoLogic is a PFIC for the taxable year during which CryptoLogic pays a dividend or for the preceding taxable year.

As discussed below, CryptoLogic does not believe that it was a PFIC for the previous taxable year. (See Passive Foreign Investment Company below). However, there can be no assurance that the IRS will not challenge the determination made by CryptoLogic concerning its PFIC status or that CryptoLogic will not be a PFIC for the current taxable year or any subsequent taxable year.

If CryptoLogic is not a QFC, a dividend paid by CryptoLogic to a U.S. Holder generally will be taxed at ordinary income tax rates (and not at the preferential tax rates applicable to long-term capital gains).

### Distributions Paid in Foreign Currency

The taxable amount of a distribution received on the CryptoLogic shares in foreign currency generally will be equal to the U.S. dollar value of such distribution based on the exchange rate applicable on the date of receipt. A U.S. Holder that does not convert foreign currency received as a distribution into U.S. dollars on the date of receipt generally will have a tax basis in such foreign currency equal to the U.S. dollar value of such foreign currency on the date of receipt. Such a U.S. Holder generally will recognize ordinary income or loss on any subsequent sale or other taxable disposition of such foreign currency (including an exchange for U.S. dollars).

### Disposition of CryptoLogic Shares

A U.S. Holder will recognize gain or loss on the sale or other taxable disposition of CryptoLogic shares in an amount equal to the difference, if any, between (a) the amount of cash plus the fair market value of any property received; and (b) such U.S. Holder's adjusted tax basis in the CryptoLogic shares sold or otherwise disposed of. Subject to the PFIC rules discussed below, any such gain or loss generally will be capital gain or loss, which will be long-term capital gain or loss if the CryptoLogic shares are held for more than one year.

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Preferential tax rates apply to long-term capital gains of a U.S. Holder that is an individual, estate, or trust. There are currently no preferential tax rates for long-term capital gains of a U.S. Holder that is a corporation. Deductions for capital losses are subject to significant limitations under the U.S. Code.

### Foreign Tax Credit

A U.S. Holder that pays (whether directly or through withholding) Irish income tax with respect to dividends received on the CryptoLogic shares generally will be entitled, at the election of such U.S. Holder, to receive either a deduction or a credit for such Irish income tax paid. Generally, a credit will reduce a U.S. Holder's

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U.S. federal income tax liability on a dollar-for-dollar basis, whereas a deduction will reduce a U.S. Holder's income subject to U.S. federal income tax. This election is made on a year-by-year basis and applies to all foreign taxes paid (whether directly or through withholding) by a U.S. Holder during a taxable year.

Complex limitations apply to the foreign tax credit, including the general limitation that the credit cannot exceed the proportionate share of a U.S. Holder's U.S. federal income tax liability that such U.S. Holder's foreign source taxable income bears to such U.S. Holder's worldwide taxable income. In applying this limitation, a U.S. Holder's various items of income and deduction must be classified, under complex rules, as either foreign source or U.S. source. In addition, this limitation is calculated separately with respect to passive category income and general category income. Gain or loss recognized by a U.S. Holder on the sale or other taxable disposition of CryptoLogic shares generally will be treated as U.S. source for purposes of applying the foreign tax credit rules unless the gain is subject to tax in Ireland and is resourced as foreign source under the Convention and such U.S. Person elects to treat such gain or loss as foreign source. Dividends received on the CryptoLogic shares generally will be treated as foreign source and generally will be categorized as passive category income. Income or loss on the sale or other taxable disposition of foreign currency will be U.S. source. The foreign tax credit rules are complicated, and each U.S. Holder should consult its own tax advisor regarding the foreign tax credit rules.

### Passive Foreign Investment Company

The foregoing discussion assumes that CryptoLogic was not a PFIC for any taxable year during which a U.S. Holder held CryptoLogic shares.

A non-U.S. corporation is classified as a PFIC for each taxable year in which (a) 75% or more of its gross income is passive income (as defined for U.S. federal income tax purposes); or (b) on average for such taxable year, 50% or more (by value) of its assets either produce or are held for the production of passive income. In addition, if a corporation is classified as a PFIC for any taxable year during which a U.S. Holder has held shares of such corporation, such corporation may continue to be classified as a PFIC for any subsequent taxable year in which the U.S. Holder continues to hold the shares even if the corporation's income and costs are no longer passive in nature in that subsequent taxable year. For purposes of the PFIC provisions, passive income generally includes dividends, interest, royalties, rents, and gains from commodities or securities transactions, including certain transactions involving oil and gas. In determining whether or not it is classified as a PFIC, a non-U.S. corporation is required to take into account its pro rata portion of the income and assets of each corporation in which it owns, directly or indirectly, at least 25% (by value) of the stock.

For purposes of the PFIC income test and asset test described above, if a corporation owns, directly or indirectly, 25% or more of the total value of the outstanding shares of another foreign corporation, it will be treated as if it (a) holds a proportionate share of the assets of such other foreign corporation and (b) receives directly a proportionate share of the income of such other foreign corporation. In addition, for purposes of the PFIC income test and asset test described above, passive income does not include any interest, dividends, rents, or royalties that are received or accrued by a corporation from a related person (as defined in Section 954(d)(3) of the Code), to the extent such items are properly allocable to the income of such related person that is not passive income.

Additionally, if a non-U.S. corporation is a PFIC and if one or more of its non-U.S. corporate subsidiaries were treated as a PFIC (lower-tier PFICs), U.S. Holders of shares of such corporation would be considered to own, and also would be subject to U.S. federal income tax on (i) a distribution on the shares of a lower-tier PFIC and (ii) a disposition of shares of a lower-tier PFIC, both as if the holder directly held the shares of such lower-tier PFIC regardless of the percentage of their ownership in the corporation. In such circumstances a U.S. Holder of common shares could elect an alternative taxation regime in respect of its indirect ownership interest in a lower-tier PFIC, subject to certain conditions as discussed below.



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### Consequences if CryptoLogic Classified as a PFIC

CryptoLogic believes that it was not a PFIC for its taxable year ending December 31, 2009. Whether CryptoLogic will be considered a PFIC for any taxable year will depend on the assets and income of CryptoLogic over the course of such taxable year. PFIC classification is fundamentally factual in nature, generally cannot be determined until the close of the taxable year in question, and is determined annually. The determination of whether CryptoLogic will be a PFIC for a taxable year depends, in part, on the application of complex U.S. federal income tax rules, which are subject to differing interpretations. Consequently, there can be no assurance that CryptoLogic has not been and will not become a PFIC during any taxable year in which U.S. Holders held CryptoLogic shares. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the status of CryptoLogic under the PFIC rules.

Whether CryptoLogic will be considered a PFIC for its current taxable year or for any subsequent taxable year, will depend on the assets and income of CryptoLogic over the course of each such taxable year and, as a result, cannot be predicted with certainty as of the date of this annual report. Accordingly, there can be no assurance that CryptoLogic will not be considered a PFIC for the taxable year that includes the day after this publication or for any subsequent taxable year. PFIC classification is fundamentally factual in nature, generally cannot be determined until the close of the taxable year in question, and is determined annually. Consequently, there can be no assurance that CryptoLogic will not be or become a PFIC for any taxable year during which U.S. Holders hold CryptoLogic shares.

If CryptoLogic is or has been classified as a PFIC for any taxable year during which a U.S. Holder holds or has held CryptoLogic shares, the U.S. federal income tax consequences to a U.S. Holder of the acquisition, ownership, and disposition of CryptoLogic shares will depend on whether such U.S. Holder makes an election to treat CryptoLogic as a qualified electing fund or QEF under Section 1295 of the Code (a QEF Election) or a mark-to-market election under Section 1296 of the Code (a Mark-to-Market Election). A U.S. Holder that does not make either a QEF Election or a Mark-to-Market Election will be referred to in this summary as a Non-Electing U.S. Holder.

Under Section 1291 of the Code, any gain recognized on the sale or other taxable disposition of CryptoLogic shares, and any excess distribution (as defined in Section 1291(b) of the Code) paid on the CryptoLogic shares, must be ratably allocated to each day in a Non-Electing U.S. Holder's holding period for the CryptoLogic shares. The amount of any such gain or excess distribution allocated to prior years of such Non-Electing U.S. Holder's holding period for the CryptoLogic shares generally will be subject to U.S. federal income tax at the highest tax applicable to ordinary income in each such prior year. A Non-Electing U.S. Holder will be required to pay interest on the resulting tax liability for each such prior year, calculated as if such tax liability had been due in each such prior year.

A U.S. Holder that makes a QEF Election generally will not be subject to the rules of Section 1291 of the Code discussed above. However, a U.S. Holder that makes a QEF Election generally will be subject to U.S. federal income tax on such U.S. Holder's pro rata share of (a) the net capital gain of CryptoLogic, which will be taxed as long-term capital gain to such U.S. Holder, and (b) and the ordinary earnings of CryptoLogic, which will be taxed as ordinary income to such U.S. Holder. A U.S. Holder that makes a QEF Election will be subject to U.S. federal income tax on such amounts for each taxable year in which CryptoLogic is a PFIC, regardless of whether such amounts are actually distributed to such U.S. Holder by CryptoLogic.

A U.S. Holder that makes a Mark-to-Market Election generally will not be subject to the rules of Section 1291 of the Code discussed above. A U.S. Holder may make a Mark-to-Market Election only if the CryptoLogic shares are marketable stock (as defined in Section 1296(e) of the Code). A U.S. Holder that makes a Mark-to-Market Election will include in gross income, for each taxable year in which CryptoLogic is a PFIC, an amount equal to the excess, if any, of (a) the fair market value of the CryptoLogic shares as of the close of such taxable year over (b) such U.S. Holder's tax basis in such CryptoLogic shares. A U.S. Holder that makes a Mark-to-Market Election will, subject to certain limitations, be allowed a deduction in an amount equal to the excess, if



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any, of (a) such U.S. Holder's adjusted tax basis in the CryptoLogic shares over (b) the fair market value of such CryptoLogic shares as of the close of such taxable year.

U.S. Holders should be aware that, in the event that CryptoLogic is or becomes a PFIC, there can be no assurance that CryptoLogic will supply U.S. Holders with the information and statements that such U.S. Holders require to make a QEF election discussed above.

The PFIC rules are complex, and each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the PFIC rules and how the PFIC rules may affect the U.S. federal income tax consequences of the acquisition, ownership, and disposition of CryptoLogic shares.

### **Backup Withholding Tax and Information Reporting Requirements**

Unless the U.S. Holder is a corporation or other exempt recipient, payments to certain U.S. Holders of dividends made on CryptoLogic shares, or the proceeds of the sale or other disposition of the CryptoLogic shares or the CryptoLogic shares that are made within the U.S. or through certain U.S. related financial intermediaries may be subject to information reporting and U.S. federal backup withholding tax at the current rate of twenty-eight percent (28%) (subject to periodic adjustment) if the U.S. Holder fails to supply a correct taxpayer identification number or otherwise fails to comply with applicable U.S. information reporting or certification requirements. Any amount withheld from a payment to a U.S. Holder under the backup withholding rules is allowable as a credit against the U.S. Holder's U.S. federal income tax, provided that the required information is furnished to the IRS.

### **IRISH INCOME TAX CONSIDERATIONS**

#### **General**

The following summary, which is intended as a general guide only, outlines certain aspects of legislation and Revenue practice in Ireland regarding the Irish taxation of dividends as applicable to U.S. and Canadian residents. It is based on existing Irish tax legislation, court decisions, the current practice of the Revenue Commissioners in Ireland and the respective double taxation agreements between Ireland and the U.S. and Ireland and Canada. This summary is not exhaustive and does not purport to deal with the Irish taxation of dividends for all categories of U.S. and Canadian resident investors, some of which may be subject to special rules such as dealers in securities.

All shareholders should seek independent advice on the tax implications arising in their own particular situations as to the taxation consequences relevant to them. Each shareholder should also understand that future legislative, administrative and judicial changes could modify the tax consequences described below, possibly with retroactive effect.

The following summary is also prepared on the basis that CryptoLogic, which is Guernsey incorporated, is tax resident in Ireland by virtue of its central management and control being situated in Ireland. However, this summary does not constitute confirmation that CryptoLogic will be solely tax resident in Ireland.

*This discussion is for general information only and it is not intended to be, nor should it be construed to be, legal or tax advice to any Irish Holder or prospective Irish Holder of shares of the Company, and no opinion or representation with respect to the Irish income tax consequences to any such Irish Holder or prospective Irish Holder is made. Accordingly, Irish Holders and prospective Irish Holders of shares of the Company should consult their own financial advisor, legal counsel or accountant regarding the Irish tax consequences of*

*purchasing, owning and disposing of shares of the Company.*

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### **Irish Taxation of Dividends for U.S. and Canadian Residents**

The following summary, which is intended as a general guide only, outlines certain aspects of legislation and Revenue practice in Ireland regarding the Irish taxation of dividends as applicable to U.S. and Canadian residents. It is based on existing Irish tax legislation, court decisions, the current practice of the Revenue Commissioners in Ireland and the respective double taxation agreements between Ireland and the U.S. and Ireland and Canada. This summary is not exhaustive and does not purport to deal with the Irish taxation of dividends for all categories of U.S. and Canadian resident investors, some of which may be subject to special rules such as dealers in securities.

All shareholders should seek independent advice on the tax implications arising in their own particular situations as to the taxation consequences relevant to them. Each shareholder should also understand that future legislative, administrative and judicial changes could modify the tax consequences described below, possibly with retroactive effect.

The following summary is also prepared on the basis that CryptoLogic, which is Guernsey incorporated, is tax resident in Ireland by virtue of its central management and control being situated in Ireland. However, this summary does not constitute confirmation that CryptoLogic will be solely tax resident in Ireland.

### Withholding Tax

All dividends paid by CryptoLogic, other than dividends paid entirely out of exempt patent income (this exemption is subject to specific conditions), will be subject to Irish withholding tax at the standard rate of income tax in force at the time the dividend is paid, currently 20%. An individual shareholder who is neither resident nor ordinarily resident for tax purposes in Ireland, but is resident in a country with which Ireland has a double tax treaty, which includes the U.S. and Canada, or in a member state of the EU, other than Ireland (together a Relevant Territory ), will be exempt from withholding tax provided he or she makes the requisite declaration.

Non-Irish resident corporate shareholders that:

- are ultimately controlled by residents of a Relevant Territory;
- are resident in a Relevant Territory and are not controlled by Irish residents;
- have the principal class of their shares, or shares of a 75% parent, substantially and regularly traded on one or more recognized stock exchanges; or
- are wholly owned by two or more companies, each of whose principal class of shares is substantially and regularly traded on one or more recognized stock exchanges;

will be exempt from withholding tax on the production of the appropriate certificates and declarations except in those circumstances where the shares are held in bare trust on behalf of the beneficial owner. In these latter circumstances, it may be possible to avoid the withholding tax with the prior approval of the Irish tax authorities if the beneficial owner is resident in a Relevant Territory and not under the control of Irish residents.

### Income Tax

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Under certain circumstances, non-Irish resident shareholders will be subject to Irish income tax on dividend income. This liability is limited to tax at the standard rate and therefore, where withholding tax has been deducted, this will satisfy the tax liability.

However, a non-Irish resident shareholder will not have an Irish income tax liability on dividends from the company if the holder is neither resident nor ordinarily resident in the Republic of Ireland and the holder is:

an individual resident in the U.S. or Canada (or any other country with which Ireland has concluded a double taxation treaty);

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a corporation that is ultimately controlled by persons resident in the U.S. or Canada (or any other country with which Ireland has concluded a double taxation treaty);

a corporation whose principal class of shares (or its 75% or greater parent's principal class of shares) is substantially and regularly traded on a recognized stock exchange in an EU country or a country with which Ireland has concluded a double taxation treaty;

a corporation resident in another EU member state or in a country with which Ireland has concluded a double taxation treaty, which is not controlled directly or indirectly by Irish residents; or

a corporation that is wholly owned by two or more corporations each of whose principal class of shares is substantially and regularly traded on a recognized stock exchange in an EU country or a country with which Ireland has concluded a double taxation treaty.

A declaration in the prescribed form and any other evidence required must be provided to establish entitlement to the exemption.

U.S. or Canadian Shareholders that do not currently fulfill the documentation requirements or otherwise do not qualify for the withholding tax exemption may be able to claim treaty benefits under the relevant treaty. The documentation requirements have changed in 2010 which streamlines the process for claiming the dividend tax exemption.

### **Irish Capital Gains Tax for U.S. and Canadian Residents**

CryptoLogic shares constitute chargeable assets for Irish capital gains tax purposes and, accordingly, Shareholders who are resident or ordinarily resident in Ireland, depending on their circumstances, may be liable to Irish tax on capital gains on a disposal of CryptoLogic shares. A Shareholder who is neither resident nor ordinarily resident in Ireland should not be liable to Irish capital gains tax on a disposal of CryptoLogic shares unless the CryptoLogic shares (i) are or were held for the purposes of a trade carried on by the shareholder in Ireland; or (ii) derive the greater part of their value from Irish land or exploration rights and are unquoted.

There are provisions to subject a person who disposes of an interest in a company while temporarily being non-Irish resident, to Irish capital gains tax. This treatment will apply to Irish domiciled individuals:

who cease to be Irish resident;

who own the shares when they cease to be resident;

if there are not more than 5 years of assessment between the last year of Irish tax residence prior to becoming temporarily non-resident and the tax year that he/she resumes Irish tax residency;

who dispose of an interest in a company during this temporary non-residence; and

the interest disposed of represents 5% or greater of the share capital of the company or exceeds 500,000 in value.

In these circumstances the person will be deemed, for Irish capital gains tax purposes, to have sold and immediately reacquired the interest in the company on the date of his or her departure and will be subject to tax at 25% of the taxable gain (the 25% rate applies to disposals made on or after April 8, 2009 while the rate is 22% for disposals made between October 15, 2008 and April 7, 2009).

**Irish Stamp Duty for U.S. and Canadian Residents**

On the basis that CryptoLogic, which is a Guernsey incorporated company, also has its registered office and maintains its share register in Guernsey, the ordinary shares of CryptoLogic should not be considered Irish property and therefore no Irish stamp duty should apply on their transfer unless:

- (i) the transfer of such shares is executed in Ireland; or
- (ii) the transfer relates to a matter or thing done or to be done in Ireland.

Even if the above circumstances i) and ii) apply, there is an exemption currently applied in practice by the Irish Revenue Commissioners to the effect that no Irish stamp duty should arise on the transfer of shares in non-Irish registered companies provided the transfer of shares is not related to immovable property in Ireland or related to shares of a company which is registered in Ireland.

Irish stamp duty is payable on transfers of ordinary shares of Irish registered companies (other than between spouses) wherever a document of transfer is executed. Where such transfers are attributable to a sale, stamp duty will be charged at a rate of one per cent., rounded to the nearest euro. The stamp duty is calculated on the amount or value of the consideration (i.e., purchase price) or, if the transfer is by way of a gift (subject to certain exceptions) or for consideration less than the market value, on the market value of the shares. Where the consideration for the sale is expressed in a currency other than euro, the duty will be charged on the euro equivalent calculated at the rate of exchange prevailing on the date of the transfer.

The person accountable for payment of stamp duty is the transferee or, in the case of a transfer by way of gift or for a consideration less than the market value, all parties to the transfer. Stamp duty is normally payable within 30 days after the date of execution of the transfer. Late or inadequate payment of stamp duty will result in liability for interest, penalties and surcharges.

**Irish Capital Acquisitions Tax for U.S. and Canadian Residents**

Irish capital acquisitions tax ( CAT ) comprises principally of gift tax and inheritance tax.

CryptoLogic shares should not be regarded as property situated in Ireland for CAT purposes on the basis the share register of CryptoLogic is not held in Ireland. However, CAT could apply to a gift or inheritance of Ordinary Shares if the donor or person who receives the gift or inheritance is resident or ordinarily resident in Ireland at the date of the gift or inheritance. The person who receives the gift or inheritance is primarily liable for CAT.

CAT is levied at a rate of 25% above certain tax-free thresholds (this rate is effective for valuation dates from April 8, 2009 and a rate of 22% applies to gifts and inheritances taken where the valuation date is between November 20, 2008 and April 7, 2009). The appropriate tax-free threshold is dependent upon: (1) the relationship between the donor and the donee; and (2) the aggregation of the values of previous gifts and inheritances received by the donee from persons within the same group threshold. Gifts and inheritances passing between spouses are exempt from CAT.

**F. DIVIDENDS AND PAYING AGENTS**

Not applicable.

**G. STATEMENT BY EXPERTS**

Not applicable.

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## **H. DOCUMENTS ON DISPLAY**

Any documents referred to in this annual report may be inspected at the Company's head office located at Marine House, Clanwilliam Place, Dublin 2, Ireland during normal business hours.

In addition, various documents referenced in this annual report are included as exhibits to this annual report in accordance with Item 19 of this Form 20-F. You may read and copy any materials we file with or furnish to the SEC at its 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. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the Public Reference Room. The SEC further maintains an internet website at [www.sec.gov](http://www.sec.gov) that contains reports and other information about issuers who submit documents electronically with the SEC.

## **I. SUBSIDIARY INFORMATION**

Not applicable.

## **ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

### **Foreign Exchange Risk**

We operate in a number of foreign jurisdictions, generate revenues and incur expenses in the currencies of these jurisdictions (U.S. Dollars, British Pounds, euro, and Canadian Dollars). Our financial results are reported in U.S. currency, which is subject to fluctuations in respect of the currencies of the countries in which we operate, including British Pounds, euro, and Canadian Dollars.

Monetary items denominated in currencies other than U.S. dollars are translated into U.S. dollars at exchange rates in effect at the balance sheet dates, and non-monetary items and related amortization are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenue and expenses other than amortization are translated at rates in effect at the time of the transactions. Foreign exchange gains and losses are included in the consolidated statements of (loss)/earnings.

We have performed sensitivity analyses as of December 31, 2009 using a modeling technique that measures the change in the fair values arising from a hypothetical 10% adverse movement in the levels of foreign currency exchange rates relative to the U.S. dollar, with all other variables held constant. The analyses cover all of our foreign currency contracts offset by the underlying exposures. The foreign currency exchange rates we used were based on market rates in effect at December 31, 2009. The sensitivity analysis indicated that a hypothetical 10% strengthening of the U.S. dollar against the euro, Canadian dollar and British pound would have increased revenues by \$2.6 million and increased expenses by \$5.4 million, therefore decreasing net income by \$2.8 million. A hypothetical 10% weakening of the U.S. dollar against the euro, Canadian dollar and British pound would have had an equal but opposite impact.

In 2009, the Company implemented a hedging program to limit the foreign exchange exposure primarily on cash outflows in Canadian Dollars as there are no offsetting revenues. At December 31, 2009, there were no open hedging instruments. In 2008 and 2007, the Company did not engage in any material hedging activities.

We may utilize a hedging program from time to time and/or take advantage of the natural hedge in having operations in multiple currencies to mitigate a portion of our currency risks, but there can be no assurance that we will not experience currency losses in the future, which could have a material adverse effect on our business, revenues, operating results and financial condition.

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**Interest Rate Risk**

Financial instruments that potentially expose the Company to a concentration of credit risk, interest rate and foreign exchange risk consist principally of cash and cash equivalents and short-term investments and user funds on deposit. The Company manages credit risk by investing in cash equivalents and short-term investments rated as A and R1 or above. Our cash and cash equivalents are primarily held in U.S. dollars, British Pounds and euro.

The Company does not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates relative to interest rates on the investments, owing to the short-term nature of the investments.

The weighted average effective interest rate on short-term investments as at December 31, 2009 is 1.24% (2008 2.53%; 2007 6.94%).

A hypothetical 100 basis point movement in our interest rate yield earned on cash and cash equivalents, security deposits, restricted cash, and user funds on deposit during the year ended December 31, 2009 would have decreased interest income by approximately \$0.4 million.

The related interest income or expense and gains and losses for financial assets classified as held-for-trading are included as interest income in the accompanying consolidated statements of earnings. Interest income or expense relating to loans and receivables and other financial liabilities are included in operating expenses in the accompanying consolidated statements of earnings.

**ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

Not applicable.

**PART II**

**ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

Not applicable.

**ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS**

Not applicable.

**ITEM 15. CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures**

Our management, under the supervision and with the participation of Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this annual report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

## **Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) under the Exchange Act as a process designed by, or under the supervision of, the issuer's principal executive officer and principal financial officer and effected by the issuer's board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. It 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 assets of the issuer, provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with Canadian GAAP and that receipts and expenditures are made only in accordance with authorization of management and the board of directors, and provide reasonable assurance regarding prevention or timely detection of the unauthorized acquisition, use or disposition of the issuer's assets that could have a material effect on the financial statements of the issuer.

It should be noted that internal control over financial reporting can provide only reasonable, not absolute, assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management, under the supervision and with the participation of Chief Executive Officer and Chief Financial Officer, assessed the effectiveness of our internal control over financial reporting as of the end of the period covered by this annual report. 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 this assessment, our management concluded that our internal control over financial reporting was effective.

The effectiveness of our internal control over financial reporting as of December 31, 2009, has been audited by Grant Thornton, independent registered public accounting firm. Grant Thornton's report on our internal control over financial reporting appears on page F-3 of this annual report.

There were no other changes in our internal control over financial reporting that occurred during the fiscal year ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

Thomas Byrne, James Wallace and Stephen Freedhoff are members of the Audit Committee of the Company's Board of Directors, who each qualify as an audit committee financial expert based on their education and experience. Messrs. Byrne, Wallace and Freedhoff are independent, as that term is defined by the NASDAQ listing standards applicable to our Company.

### **ITEM 16B. CODE OF ETHICS**

Our Board of Directors has adopted a Code of Business Conduct and Ethics applicable to our directors, officers (including our principal executive officer, our principal financial officer, and our principal accounting officer), employees, contractors, and other representatives. The Code of Business Conduct and Ethics summarizes the legal, ethical, and regulatory standards applicable to our Company. A copy of the Code of Business Conduct and Ethics is available on our web site at [www.cryptologic.com](http://www.cryptologic.com).



**ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

On October 27, 2008, the Company announced the appointment of Grant Thornton as independent auditor, succeeding KPMG LLP. Fees billed for audit and non-audit services in connection with the fiscal years ended December 31, 2009 and 2008 are outlined in the following table (in thousands of U.S. dollars):

	2009	2008 <sup>(1)</sup>
Audit Fees	\$1,262	\$1,118
Audit-Related Fees		\$109
Tax Fees	\$126	\$969
All Other Fees		\$603
Total	\$1,388	\$2,799

<sup>(1)</sup> The audit fees of \$1,118 related to services performed by Grant Thornton and the remaining non audit fees of \$1,681 relate to services performed by KPMG LLP.

*Audit Fees*

Audit fees were for professional services rendered for the audits of the Company's consolidated financial statements and subsidiary companies, the review of interim financial statements, the review of accounting disclosure requirements regarding other business activities and review of documents filed with U.S., Canadian and U.K. securities regulatory authorities including documents relating to the Company's reorganization to Ireland.

*Audit-Related Fees*

Audit-related fees were for advisory services related to Sarbanes-Oxley and other related compliance matters.

*Tax Fees*

Tax fees were for tax compliance, tax advice and tax planning. These services included the preparation and review of corporate tax returns, assistance with tax audits and transfer pricing matters, expatriate advisory services as well as advisory services relating to the Company's reorganization to Ireland, federal, provincial and international tax compliance for customs and duties, and regarding common forms of domestic and international taxation (i.e., income tax, VAT, GST and excise taxes).

*All Other Fees*

Other fees were for services other than audit fees, audit-related fees and tax fees as described above. These services included probity checks of employees and licensees.

**Pre-Approval Policies and Procedures**

The Company's Audit Committee has concluded that the provision of services other than audit services is compatible with maintaining auditor independence. The Audit Committee monitors audit functions and the preparation of financial statements, and meets with external auditors independent of management. The Audit Committee has adopted a policy regarding its pre-approval of all audit and permissible non-audit services provided by the independent auditors. The policy gives guidance to the Company's management as to the specific types of services that have been pre-approved. The Company's senior management periodically provides the Audit Committee with a summary of services provided by the independent auditors in accordance with the pre-approval policy. For the year ended December 31, 2009, none of the audit-related, tax and other fees described above were an exception to the Audit Committee's pre-approval policy.

**ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not applicable.

**ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
January 1-31, 2008				1,281,000
February 2-29, 2008				1,281,000
March 1-31, 2008				1,281,000
April 1-30, 2008				1,281,000
May 1-31, 2008				1,281,000
June 1-30, 2008	48,920	\$15.12	48,920	1,232,080
July 1-31, 2008	21,830	13.70	21,830	1,210,250
August 1-31, 2008	12,465	10.10	12,465	1,197,785
September 1-30, 2008	31,825	6.32	31,825	1,165,960
October 1-31, 2008	9,865	5.52	9,865	1,156,095
November 1-30, 2008				1,156,095
December 1-31, 2008				1,267,871
Total	124,905	\$11.37	124,905	

In November 2007, we initiated a Normal Course Issuer Bid (the 2008 Normal Course Issuer Bid ) that entitled us to acquire and cancel up to 1,281,000 of our common shares between November 14, 2007 and November 13, 2008. All purchases are to be made on the open market at the market price at the time of the purchase. For the year ended December 31, 2008, we repurchased 124,905 shares, for a total cost of \$1.4 million associated with the 2008 Normal Course Issuer Bid.

In November 2008, we initiated a Normal Course Issuer Bid (the 2009 Normal Course Issuer Bid ), which authorizes us to acquire and cancel up to 1,267,871 of its common shares between December 3, 2008 and December 2, 2009. At December 31, 2009, there were no purchases under the 2009 Normal Course Issuer Bid.

The Company did not repurchase any shares during 2009.

**ITEM 16F. CHANGE IN REGISTRANT S CERTIFYING ACCOUNTANT**

Not applicable

**ITEM 16G. CORPORATE GOVERNANCE**

NASDAQ Listing Rule 5615(a)(3) permits foreign private issuers such as us to follow home country corporate governance practices in lieu of certain NASDAQ requirements. A significant way in which our governance practices differ from those followed by U.S. domestic companies listed on NASDAQ relates to the shareholder meeting quorum requirement. Under our Articles, the holders of not less than 25 percent of the shares entitled to vote at a meeting of shareholders present in person or by proxy constitutes a quorum for the transaction

of business at any meeting of shareholders. By contrast, under NASDAQ Listing Rule 5620(c), the minimum quorum requirement should not be less than 33 1/3 percent of the outstanding shares of a listed company's common voting stock.

**PART III**

**ITEM 17. FINANCIAL STATEMENTS**

The following financial statements and schedule, together with the reports of Grant Thornton and KPMG LLP thereon, are filed as part of this annual report:

Management's Responsibility For Financial Reporting	F-1
Report of Independent Registered Public Accounting Firm	F-2
Report of Independent Registered Public Accounting Firm	F-3
Report of Independent Registered Public Accounting Firm	F-4
Consolidated Balance Sheets	F-5
Consolidated Statements of (Loss)/Earnings and Comprehensive (Loss)/Income	F-6
Consolidated Statements of (Deficit)/Retained Earnings	F-7
Consolidated Statements of Cash Flows	F-8
Notes to Consolidated Financial Statements	F-9
Schedule II - Valuation and Qualifying Accounts	S-1

**ITEM 18. FINANCIAL STATEMENTS**

Not applicable.

**ITEM 19. EXHIBITS**

The following exhibits are filed or furnished as part of this annual report:

- 1.1 Memorandum of Association of CryptoLogic Limited (incorporated by reference to Exhibit 1.1 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 1.2 Articles of Association of CryptoLogic Limited (incorporated by reference to Exhibit 1.2 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 3.1 Voting and Exchange Trust Agreement dated April 20, 2007 among CryptoLogic Exchange Corporation, CryptoLogic Limited, and Equity Trust & Transfer Co.
- 4.1 Shareholders Agreement dated May 9, 2008 among CryptoLogic (Asia Pacific) Pte Ltd, Jingle Prize, Inc., and various listed persons (incorporated by reference to Exhibit 4.17 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 4.2 Employment Agreement dated February 27, 2008 between CryptoLogic Limited and Brian Hadfield (incorporated by reference to Exhibit 4.11 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 4.3 Amending Agreement dated November 11, 2008 to Employment Agreement dated February 27, 2008 between CryptoLogic Limited and Brian Hadfield
- 4.4 Second Amending Agreement dated January 13, 2009 to Employment Agreement dated February 27, 2008 between CryptoLogic Limited and Brian Hadfield
- 4.5 Employment Agreement dated June 1, 2007 between CryptoLogic Limited and Stephen Taylor (incorporated by reference to Exhibit 4.13 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 4.6 Consulting Agreement dated June 1, 2007 between Westbury Marketing Ltd. and Stephen Taylor (incorporated by reference to Exhibit 4.14 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 4.7 Consulting Agreement dated June 1, 2007 between CryptoLogic Limited and Westbury Marketing Ltd. (incorporated by reference to Exhibit 4.15 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 4.8 Consulting Agreement dated June 1, 2007 between Game Pack and Westbury Marketing Ltd. (incorporated by reference to Exhibit 4.16 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 4.9 Long-Term Incentive Plan effective January 1, 2005 (incorporated by reference to Exhibit 4.3 to our Annual Report on Form 20-F for the fiscal year ended December 31, 2007 filed May 20, 2008)
- 8.1 List of Subsidiaries of CryptoLogic Limited
- 12.1 Certification of the Principal Executive Officer of CryptoLogic Limited filed pursuant to Section 302 of Sarbanes-Oxley Act of 2002
- 12.2 Certification of the Principal Financial Officer of CryptoLogic Limited filed pursuant to Section 302 of Sarbanes-Oxley Act of 2002
- 13.1 Certification of the Principal Executive Officer of CryptoLogic Limited furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 13.2 Certification of the Principal Financial Officer of CryptoLogic Inc. furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

**SIGNATURES**

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

**CRYPTOLOGIC LIMITED**

Date: March 30, 2010  
Brian Hadfield

By /s/ Brian Hadfield

President and Chief Executive Officer

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Consolidated Financial Statements

(In U.S. dollars)

# **CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Years ended December 31, 2009, 2008 and 2007

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## MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of CryptoLogic Limited and its subsidiaries and all the information in Management's Discussion and Analysis are the responsibility of management and have been approved by the Board of Directors.

The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. These statements include some amounts that are based on best estimates and judgement. Management has determined such amounts on a reasonable basis in order to ensure that the consolidated financial statements are presented fairly, in all material respects. Management has prepared the financial information presented elsewhere in Management's Discussion and Analysis and has ensured that it is consistent with the consolidated financial statements.

The Company policy is to maintain systems of internal accounting and administrative controls of high quality consistent with reasonable cost. Such systems are designed to provide reasonable assurance that the financial information including the preparation of the consolidated financial statements and accompanying notes is relevant, accurate and reliable and that the Company's assets are appropriately accounted for and adequately safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for approving the consolidated financial statements. The Board carries out this responsibility through its Audit Committee.

The Audit Committee is appointed by the Board and is comprised of a majority of outside Directors. The Committee meets periodically with management and the external auditors to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues to satisfy itself that each party is properly discharging its responsibilities. The Audit Committee reviews the Company's annual consolidated financial statements, the external auditors' report and other information in the Annual Report. The Audit Committee reports its findings to the Board for consideration by the Board when it approves the consolidated financial statements for issuance to the shareholders. The Committee also considers, for review by the Board of Directors and approval by the shareholders, the engagement or re-appointment of the external auditors.

On behalf of the shareholders, the 2009 consolidated financial statements have been audited by Grant Thornton, the external auditors, in accordance with the standards of the Public Company Accounting Oversight Board (United States). Grant Thornton has full and free access to the Audit Committee.

/s/ Brian Hadfield  
President and Chief Executive Officer

/s/ Stephen Taylor  
Chief Financial Officer

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**THE BOARD OF DIRECTORS AND SHAREHOLDERS OF CRYPTOLOGIC LIMITED (FORMERLY CRYPTOLOGIC INC.)**

We have audited the accompanying consolidated balance sheets of CryptoLogic Limited (formerly CryptoLogic Inc.) as at December 31, 2009 and 2008 and the consolidated statements of (loss)/earnings and comprehensive (loss)/income, (deficit)/retained earnings, and cash flows for each of the years in the two year period ended December 31, 2009. Our audits of the basic financial statements included the financial statement schedule II. These consolidated financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform an audit to obtain reasonable assurance 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. An audit also includes 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 CryptoLogic Limited as at December 31, 2009 and 2008 and the results of its operations and cash flows for each of the years in the two year period ended December 31, 2009 in accordance with Canadian generally accepted accounting principles. Canadian generally accepted accounting principles vary in certain respects from those generally accepted in the United States of America. Information related to the nature and effect of such differences is presented in note 21 to the consolidated financial statements. Also, in our opinion, the related schedule II, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects, the information set forth herein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), CryptoLogic Limited's internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 30, 2010 expressed an unqualified opinion on the effectiveness of internal controls over financial reporting.

Chartered Accountants

Dublin, Ireland

March 30, 2010



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**THE BOARD OF DIRECTORS AND SHAREHOLDERS OF CRYPTOLOGIC LIMITED (FORMERLY CRYPTOLOGIC INC.)**

We have audited CryptoLogic Limited's (the "Company") (formerly CryptoLogic Inc.) internal control over financial reporting as of December 31, 2009, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). CryptoLogic's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on CryptoLogic's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, CryptoLogic Limited maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on criteria established in Internal Control — Integrated Framework issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of CryptoLogic Limited (formerly CryptoLogic Inc.) as at December 31, 2009 and 2008 and the consolidated statements of (loss)/earnings and comprehensive (loss)/income, (deficit)/retained earnings, and cash flows for each of the years in the two year period ended December 31, 2009 and our report dated March 30, 2010 expressed an unqualified opinion on those consolidated financial statements.

Chartered Accountants

Dublin, Ireland

March 30, 2010



## **AUDITORS' REPORT TO THE SHAREHOLDERS**

We have audited the consolidated balance sheet of CryptoLogic Limited (formerly CryptoLogic Inc.) as at December 31, 2007 and the consolidated statement of earnings and comprehensive income, retained earnings and cash flows for the year ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2007 in accordance with Canadian generally accepted accounting principles.

Chartered Accountants, Licensed Public Accountants

Toronto, Canada

March 17, 2008

**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

## Consolidated Balance Sheets

(In thousands of U.S. dollars)

December 31, 2009 and 2008

	2009	2008
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 23,447	\$ 36,348
Restricted cash (note 2)		7,175
Security deposits (note 2)	250	250
Accounts receivable and other	7,972	6,002
Income taxes receivable (note 16)	681	653
Prepaid expenses	9,426	6,564
	41,776	56,992
User funds held on deposit (note 3)	7,929	10,833
Future income tax (note 16)	1,549	1,930
Capital assets (note 4)	7,774	18,703
Long-term investments (note 5)		5,821
Intangible assets (note 6)	4,342	4,982
Goodwill (note 6)		6,545
	\$ 63,370	\$ 105,806
<b>Liabilities and Shareholders Equity</b>		
Current liabilities:		
Accounts payable and accrued liabilities (note 11)	\$ 13,156	\$ 15,356
Income taxes payable (note 16)	2,157	413
	15,313	15,769
User funds held on deposit (note 3)	7,929	10,833
Future income tax (note 16)	384	382
	23,626	26,984
Minority interest (note 7)	2,948	6,382

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Shareholders' equity: (note 8)		
Share capital (note 9)	33,916	33,552
Stock options (note 10)	7,633	6,856
(Deficit)/retained earnings	(4,753)	32,032
	<hr/>	<hr/>
	36,796	72,440
Commitments and contingencies (note 11)		
Canadian and United States accounting policy differences (note 21)		
	<hr/>	<hr/>
	\$ 63,370	\$ 105,806
	<hr/>	<hr/>

See accompanying notes to consolidated financial statements.

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On behalf of the Board:

/s/ David Gavagan  
/s/ Stephen Taylor

Director, Chairman  
Director

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

## Consolidated Statements of (Loss)/Earnings and Comprehensive (Loss)/Income

(In thousands of U.S. dollars, except per share disclosure)

Years ended December 31, 2009, 2008 and 2007

	2009	2008	2007
Revenue (note 19)	\$ 39,794	\$ 61,526	\$ 73,659
Expenses:			
Operating	39,867	55,645	49,436
General and administrative	10,181	13,660	10,166
Reorganization (note 13)	7,111	1,390	5,666
Goodwill impairment (note 6)	6,545		
Asset impairments (notes 4 and 5)	8,987	16,094	
Poker room integration costs (note 15)		3,124	
Departure costs for former CEO (note 14)		3,400	
Finance	83	359	550
Amortization	4,856	5,931	6,566
	77,630	99,603	72,384
(Loss)/earnings before the undernoted	(37,836)	(38,077)	1,275
Interest income	446	2,077	6,217
Non operating income (note 20)		102	
(Loss)/earnings before income taxes and minority interest	(37,390)	(35,898)	(35,898)
Income taxes charge/(recovery) (note 16):			
Current	664	542	4,056
Future	419	(1,026)	(3,063)
	1,083	(484)	993
(Loss)/earnings before minority interest	(38,473)	(35,414)	6,499
Minority interest (note 7)	(2,963)	(2,676)	971
Net (loss)/earnings and comprehensive (loss)/income	\$ (35,510)	\$ (32,738)	\$ 5,528
(Loss)/earnings per common share (note 12):			
Basic	\$ (2.78)	\$ (2.55)	\$ 0.47
Diluted	\$ (2.78)	\$ (2.55)	\$ 0.47

See accompanying notes to consolidated financial statements.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Consolidated Statements of (Deficit)/Retained Earnings

(In thousands of U.S. dollars)

Years ended December 31, 2009, 2008 and 2007

	<b>2009</b>	<b>2008</b>	<b>2007</b>
Retained earnings, beginning of year	\$ 32,032	\$ 70,855	\$ 78,857
Net (loss)/earnings	(35,510)	(32,738)	5,528
Dividends paid, excluding those paid to CEC shareholders	(1,275)	(4,992)	(6,408)
Reduction due to minority interest (note 7)			(7,122)
Excess of purchase price of treasury shares over stated value		(1,093)	
(Deficit)/retained earnings, end of year	\$ (4,753)	\$ 32,032	\$ 70,855

See accompanying notes to consolidated financial statements.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

## Consolidated Statements of Cash Flows

(In thousands of U.S. dollars)

Years ended December 31, 2009, 2008 and 2007

	2009	2008	2007
<b>Cash flows (used in)/provided by operating activities:</b>			
Net (loss)/earnings	\$ (35,510)	\$ (32,738)	\$ 5,528
Adjustments to reconcile earnings to cash (used in)/provided by operating activities:			
Amortization	4,856	5,931	6,566
Asset impairments	8,987	16,094	
Goodwill impairment	6,545		
Poker room integration costs		3,124	
Reorganization costs to be paid	2,924	658	
Impairments of capital assets	4,020		
Unrealized (gain)/loss on forward contract	(252)	536	
Future income taxes	419	(1,026)	(3,063)
Minority interest	(2,963)	(2,676)	971
Stock options	777	1,895	3,714
	(10,197)	(8,202)	13,716
<b>Change in operating assets and liabilities:</b>			
Accounts receivable and other	(1,766)	2,821	(3,106)
Prepaid expenses	(2,610)	1,212	(1,285)
Accounts payable and accrued liabilities	(5,211)	(9,434)	(23,612)
Income taxes payable	2,011	(4,988)	2,402
	(17,773)	(18,591)	(11,885)
<b>Cash flows used in financing activities:</b>			
Dividends paid, including those paid to CEC shareholders	(1,381)	(5,426)	(6,678)
Issue of capital stock		189	3,878
Repurchase of capital stock		(1,419)	
	(1,381)	(6,656)	(2,800)
<b>Cash flows provided by/(used in) investing activities:</b>			
Purchase of capital assets	(445)	(4,535)	(13,057)
Purchase of long-term investments	(477)	(2,695)	(5,326)
Decrease/ (increase) in restricted cash	7,175	13,401	(20,576)
Cash paid for Casino.co.uk		(1,254)	(6,098)
Decrease in security deposits		1,250	
Cash paid for acquisition of Parbet.com			(11,770)
Proceeds from sale of short-term investments			50,000

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	<b>2009</b>	<b>2008</b>	<b>2007</b>
	6,253	6,167	(6,827)
<hr/>			
Decrease in cash and cash equivalents	(12,901)	(19,080)	(21,512)
Cash and cash equivalents, beginning of year	36,348	55,428	76,940
<hr/>			
Cash and cash equivalents, end of year	\$ 23,447	\$ 36,348	\$ 55,428
<hr/>			
Supplemental cash flow information:			
Income taxes paid/(refunds received), net	\$ (1,051)	\$ 4,763	\$ 1,842
Interest received	388	1,637	6,243
Non-cash portion of options exercised		83	1,883

See accompanying notes to consolidated financial statements.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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CryptoLogic Limited and its subsidiaries (the "Company") is a provider of commerce-enabling technology, permitting secure, reliable, high-speed and private financial transactions over the Internet. The Company provides a comprehensive solution including software, network operations, administrative and marketing consulting services to licensed gaming operators. The Company also licenses individual games, generally with branded content, to licensed gaming operators ("Branded Games"). The Company earns substantially all of its revenue from the hosting and service arrangements for the operation of online casino and poker games on behalf of licensed casinos and licensing Branded Games to licensed operators. Substantially all of the Company's revenue is earned in U.S. dollars, British pounds and euro from licensees located outside of North America. Revenue from the top seven licensees constituted 82% (2008: 81%; 2007: 79%) of revenue. The Company's functional currency is the U.S. dollar and, consequently, it measures and reports its results in U.S. dollars.

Pursuant to a business reorganization implemented by way of an Ontario, Canada Superior Court of Justice court approved plan of arrangement (the "Arrangement") and approved by the shareholders on May 24, 2007, CryptoLogic Limited acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement, became an indirect subsidiary of CryptoLogic Limited. As part of the Arrangement, CryptoLogic Limited issued either an equivalent amount of its common shares or, in the case of taxable Canadian residents, exchangeable shares of CryptoLogic Exchange Corporation ("CEC"), an indirect subsidiary of CryptoLogic Limited. The CEC shares are, as nearly as practicable, the economic equivalent of CryptoLogic Limited shares. These CEC shares participate equally in voting and dividends with the shareholders of the Company. No additional shares of CEC will be issued after June 1, 2007.

For accounting purposes, the Arrangement has been accounted for using the continuity of interest method, which recognizes CryptoLogic Limited as the successor entity to CryptoLogic Inc. Accordingly, these consolidated financial statements reflect the financial position, results of operations and cash flows as if the Company has always carried on the business formerly carried on by CryptoLogic Inc. and its subsidiaries, with all assets and liabilities recorded at the carrying values of CryptoLogic Inc. The interest held by CEC shareholders has been presented as a minority interest in these consolidated financial statements, as required under Canadian generally accepted accounting principles ("Canadian GAAP") (note 7).

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies:

The consolidated financial statements are prepared in accordance with Canadian GAAP. Note 21 describes and reconciles the significant measurement differences between Canadian and U.S. GAAP affecting the accompanying consolidated financial statements. Certain amounts included in the comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current year consolidated financial statements. A summary of significant accounting policies is set out below:

(a) Basis of presentation:

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

(b) Revenue recognition:

The Company earns its revenue primarily from:

- hosting and services arrangements related to the design and operation of casino and poker sites on the internet on behalf of licensed operators (“Hosted Casino”);
- licensing individual games, generally with branded content to licensed operators (“Branded Games”);
- advertising revenue generated on websites operated by the company; and
- customizing its software for specific licensees and commerce-based transactions.

Revenues from Hosted Casino and Branded Games are recognized as the services are performed, on a daily basis, at the time of the gaming transactions, pursuant to the agreements with the licensees in which the Company participates in a pro rata share of the daily gaming profits, net of certain shared expenses (e.g. promotion costs). In addition, the Company generally receives a standard monthly fee for the provision of hosting and related services from Hosted Casino licensees.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

Advertising revenues, which are included in other revenue, are generated by display advertising on casino.co.uk and winneronline.com. Revenue is earned and recognized as “impressions” are delivered, “click-throughs” occur or “affiliate revenue” is generated. An “impression” is delivered when an advertisement appears in pages viewed by users. A “click-through” occurs when a user clicks on an advertiser’s listing. “Affiliate revenue” is generated when a player is referred from one of the company’s advertising portals to a separate online gaming site and earns a percentage of the revenue generated by that player.

Revenue from the initial customization of the software graphics, sound and texts to the specifications of the licensees, or other services contemplated at the date the contract was executed is recognized on a straight-line basis over the term of the hosting and services agreements. Revenue from customizations ordered subsequent to and not contemplated at the contract date are generally considered as a separate unit of accounting and recognized as the work is performed.

Interest income is recognized on an accrual basis.

### (c) Cash and cash equivalents:

Cash and cash equivalents include highly liquid investments which are readily convertible into known amounts of cash that generally have maturity dates of 90 days or less. As described in note 1 (e), cash and cash equivalents are stated at fair value as at December 31, 2009 and 2008.

### (d) Royalties:

The Company licenses various royalty rights, generally on an exclusive basis, for branded content to use in Internet casino games. At December 31, 2009 the company licensed rights from DC Comics, Paramount Digital Entertainment, Marvel, King Kong, and Jenga among others. Royalties are calculated using the percentage of gross revenue generated as agreed. Generally these arrangements include material prepayment of royalties. These prepaid amounts are amortized over the life of the arrangement as gross revenue is generated or on a straight line basis if the underlying games are expected to have an effective royalty rate greater than the agreed amount. The amortization of these royalties is recorded as a reduction of revenue in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/Income.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

### (e) Financial instruments:

Effective January 1, 2007, the Company adopted Canadian Institute of Chartered Accountants' ("CICA") Handbook Section 1530, Comprehensive Income ("Section 1530"); Section 3855, Financial Instruments - Recognition and Measurement ("Section 3855"); Section 3861, Financial Instruments - Disclosure and Presentation ("Section 3861"); and Section 3251, Equity. These sections provide standards for recognition, measurement, disclosure and presentation of financial assets, financial liabilities and non-financial derivatives.

Section 1530 provides standards for the reporting and presentation of comprehensive income, which represents the change in equity from transactions and other events and circumstances from non-owner sources. Comprehensive income refers to items recognized in comprehensive income that are excluded from net income calculated in accordance with Canadian GAAP. The impact of adopting the accounting for financial instruments did not have a material impact on the Company's results of operations.

On January 1, 2008 the Company adopted CICA Handbook Section 3862, Financial Instruments – Disclosure ("Section 3862"); Section 3863, Financial Instruments – Presentation ("Section 3863") and Section 1535, Capital Disclosures ("Section 1535").

Section 3862 requires disclosure in the financial statements that enables users to evaluate the significance of financial instruments for a company's financial position and performance, the nature and extent of risks arising from financial instruments to which a company is exposed during the period and at the balance sheet date, and how the Company manages those risks. The adoption of section 3862 did not have a material impact on the Company's financial statements in either the current or prior periods.

In June 2009, the CICA amended Section 3862, "Financial Instrument – Disclosures", to include additional disclosure requirements over fair value measurement for financial instruments and liquidity risk disclosures including the introduction of a three-level hierarchy that reflects information inputs used in making the fair value measurements. Level 1 is reserved for quoted prices in active markets for identical assets or liabilities, level 2 is reserved for information other than quoted prices observed in an active market and level 3 are for informational inputs that are not based on observable market data. Fair value measurements that relied on level 3 data also require the disclosure of the valuation technique used. The Company has recorded fair value measurements on its long-term investments. See note 5 for the required disclosures.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## **1. Significant accounting policies (continued):**

Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. This Section complements the existing Handbook Section 3861, Financial Instruments - Disclosure and Presentation and applies to certain liability instruments issued by a company. The adoption of section 3863 did not have a material impact on the Company's financial statements in either the current or prior periods.

Section 1535 establishes standards for disclosing information about an entity's capital and how it is managed. See note 8 for the required disclosure.

In January 2009, the Accounting Standards Board ("AcSB") issued Emerging Issues Committee 173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities ("EIC-173") that provided guidance on the recognition and measurement of certain financial assets and financial liabilities carried at fair value in accordance with Section 3855. EIC-173 concluded that the fair value of financial assets and financial liabilities, including derivative instruments, must take into account the Company's credit risk as well as the counterparty. EIC-173 must be applied retroactively without restatement of prior periods. The adoption of EIC-173 did not have a material impact on the Company's financial statements in either the current or prior periods.

### Financial assets held-for-trading

The Company classifies all cash, cash equivalents, short-term investments and user funds on deposit as held-for-trading assets, which are measured at fair value and the changes in fair value are recognized in earnings. Transaction costs related to financial assets and financial liabilities that are designated as held-for-trading are expensed as incurred.

### Loans and receivables

Accounts receivable and other are classified as loans and receivables and are recorded at amortized cost. The Company has determined that the carrying value represents fair value as at December 31, 2009 and December 31, 2008.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**1. Significant accounting policies (continued):**Financial liabilities recorded at amortized cost

All accounts payable, accrued liabilities and liabilities for user funds held on deposit are recorded at their amortized cost. The Company has determined that the carrying value represents fair value as at December 31, 2009 and December 31, 2008.

Financial assets available-for-sale

Long-term investments are classified as available-for-sale assets which are measured at fair value. Temporary changes in fair value of long-term investments are recognized in comprehensive income. Changes in fair value of long-term investments deemed to be other than temporary are recorded in the consolidated statements of (loss)/earnings and comprehensive (loss)/income. Transaction costs related to available-for-sale assets are included in the carrying value of the asset.

Section 3855 requires the Company to identify derivative instruments embedded in non-derivative contracts ("Embedded Derivatives") that require separation from the host contract and measure those Embedded Derivatives at fair value. Subsequent changes in fair value of Embedded Derivatives are recognized in earnings in the year the change occurs.

## (f) Capital assets:

Capital assets are stated at cost less accumulated amortization. Once an asset is put into use, amortization is based on the estimated useful lives of the assets using the following methods and annual rates:

Asset	Basis	Rate
Computer equipment	Diminishing balance	40%
Office furniture and equipment	Diminishing balance	25%
Computer software and licenses	Straight line	3 - 5 years
Capitalized software developmen	Straight line	7 years
Leasehold improvements	Straight line	Term of Lease

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

### (g) Software development:

Costs related to the development of software are expensed as incurred unless such costs meet the criteria for capitalization under Canadian GAAP. The Company capitalizes certain computer software development costs incurred for products designed for internal use. Capitalized software development costs are included in capital assets.

### (h) Provision for jackpots:

Several of the Company's licensees participate in progressive jackpot games. Each time a progressive jackpot game is played, a preset amount is added to a cumulative jackpot for that specific game. Once a jackpot is won, the progressive jackpot game is reset with a predetermined amount. The Company is liable for funding the jackpot wins as well as amounts required to reset the progressive jackpot game from the pool of funds collected and accrues the jackpot amount for all games on a monthly basis. The reset amount is accrued, up to the predetermined amount, as wagering occurs. The accrual for the jackpot at the consolidated balance sheet dates is included in accounts payable and accrued liabilities.

The Company regularly performs an analysis of the accumulation of jackpot funds and amounts required to address jackpot payouts. During the fourth quarter of 2009, as part of the statistical analysis of the amounts required for jackpot resets, the Company revised its estimated liability arising from the cumulative jackpot. The change in accounting estimate resulted in the reduction of the liability for jackpot accrual and a corresponding increase in revenue of \$841.

At December 31, 2009, accounts payable and accrued liabilities include \$3,020 in jackpot provisions (2008: \$3,152). This amount is sufficient to cover the full amount of any required pay-out.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

### (i) Income taxes:

The Company uses the asset and liability method of accounting for income taxes. Future income 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. Future income tax assets and liabilities are measured using enacted or substantively 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 future income tax assets and liabilities of a change in tax rates is recognized in earnings in the year that includes the enactment or substantive enactment date.

### (j) Stock-based compensation:

#### (i) Stock options:

The Company has a stock option plan for directors, officers and other key employees. The Company applies the fair value method to all grants of stock options. Stock option grants are accounted for as capital transactions at the time of the grant and are reflected as stock options in shareholders' equity. The fair value of options granted is estimated at the date of grant using the Black-Scholes option pricing model incorporating assumptions regarding risk-free interest rates, dividend yield, volatility factor of the expected market price of the Company's stock and the expected life of the options. The estimated fair value of the options is recorded in the consolidated statements of (loss)/earnings and comprehensive (loss)/income as stock compensation expense over the options' vesting periods. Upon exercise of stock options, the accumulated stock compensation expense recorded and the consideration paid are credited to share capital.

#### (ii) Long-term incentive plan:

From January 1, 2005 to January 31, 2007, the Company offered long-term incentive plans for its officers and directors (the "Plans"). The Plans provide for the granting of performance share units to retain certain individuals and reward participants for achieving various targets including, but not limited to, the growth in the Company's earnings per share, and share price, with vesting generally over a three-year performance period.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

When the performance and vesting criteria are met, the awards are settled in cash. The liability for these awards is recognized if the Company determines that it is probable that the targets of the Plans will be achieved and are included in accounts payable and accrued liabilities on the consolidated balance sheets.

Changes in this liability, which arise from fluctuations in the Company's stock price and estimated future diluted earnings per share, are recorded in operating costs over the vesting period.

### (k) Employee Benefits

The company contributes to a defined contribution pension plan on behalf of certain employees. Obligations for contributions to defined contribution pension plans are recognized as an expense in the consolidated statements of (loss)/earnings and comprehensive (loss)/income when they are due.

### (l) Foreign currency translation:

Monetary items denominated in currencies other than U.S. dollars are translated into U.S. dollars at exchange rates in effect at the balance sheet dates, and non-monetary items and related amortization are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenue and expenses other than amortization are translated at rates in effect at the time of the transactions. Foreign exchange gains and losses are included in the consolidated statements of (loss)/earnings and comprehensive (loss)/income.

### (m) Goodwill and intangible assets:

The Company adopted CICA Handbook Section 3064, Goodwill and Intangible Assets ("Section 3064"), effective from January 1, 2009, which converges accounting for goodwill and intangible assets under Canadian GAAP with International Financial Reporting Standards. The new standard provides more comprehensive guidance on intangible assets, particularly for internally developed intangible assets. The adoption of Section 3064 did not have a material impact on the Company's financial statements in either the current or prior periods.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**1. Significant accounting policies (continued):**

Intangible assets consist of customer lists, brand names and domain names acquired and are initially carried at cost. The carrying value of intangible assets is reviewed if indications of impairment exist. See note 6 for further discussion. Intangible assets are amortized on a straight-line basis over the useful lives of the respective assets as follows:

Customer lists	3 - 7 years
Brand names	12 years
Domain names	12 years

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less assumed liabilities, based on their fair values.

Goodwill is not amortized and is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting unit is compared with its fair value. When the fair value exceeds its carrying amount, goodwill is considered not to be impaired and the second step of the impairment test is unnecessary. The second step is carried out when the carrying amount of the reporting unit exceeds its fair value, in which case, the implied fair value of the goodwill is compared with its carrying amount to measure the amount of the impairment loss, if any. The implied fair value of goodwill is determined in the same manner as the value of goodwill is determined in a business combination described in the preceding paragraph, using the fair value of the reporting unit as if it were the purchase price. When the carrying amount of goodwill exceeds the implied fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess and is presented as a separate line item in the consolidated statements of (loss)/earnings and comprehensive (loss)/income.

For the year ended December 31, 2009 the Company assessed impairment of goodwill and has determined that it was impaired by \$6,545 (December 31, 2008 and 2007 no impairment in value). See note 6 for discussion.

# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

### (n) Earnings per common share:

Shares of the Company and of CEC are participating securities and, accordingly, earnings per share is calculated using the two class method. The two class method determines earnings per share for the Company's common shares and CEC shares according to dividends declared and participation rights in undistributed earnings, which in the case of the Company are equal. The Company uses the treasury stock method in computing diluted earnings per common share. The treasury stock method is a method of recognizing the use of proceeds that could be obtained upon the exercise of options and warrants in computing diluted earnings per common share. It assumes that any proceeds would be used to purchase the Company's common shares at the average market price.

### (o) Variable interest entities:

Variable interest entities ("VIEs") include entities in which holders of the equity investment at risk lack the characteristics of a controlling financial interest or the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support by other parties. Entities meeting these criteria are consolidated by the primary beneficiary.

Management assessed the Company's operations and relationships and concluded that there are no VIEs in respect of which the Company is the primary beneficiary. Accordingly, no VIEs are consolidated.

### (p) Use of estimates:

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities, including, but not limited to, the jackpot provision, the estimated useful lives of tangible and intangible assets, stock-based compensation, recoverability of future tax assets and liabilities and the reported amounts of revenue and expenses. Actual amounts could differ from those estimates.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 1. Significant accounting policies (continued):

The Company regularly performs analyses of the accumulation of jackpot funds and amounts required to address jackpot payouts and resets. During the fourth quarter of 2009, as part of the statistical analysis of the amounts required for jackpot resets, the Company revised its estimated liability arising from the cumulative jackpot. The change in accounting estimate resulted in the reduction of the liability for jackpot accrual and a corresponding increase in revenue of \$841. The effect on future periods resulting from the change in accounting estimate is not readily determinable as it is dependant on the timing of jackpot wins.

During the third quarter of 2009, the Company revised its estimate for liabilities in respect of intellectual property matters based on new facts and circumstances including changes to the relevant case law resulting in a reduction in accrued liabilities and a corresponding increase in revenue of \$750.

During the first quarter of 2008, the Company revised its estimate liabilities in respect of intellectual property matters based on new facts and circumstances including recent negotiations resulting in a reduction in accrued liabilities and a corresponding increase in revenue of \$1,000.

During 2009 and 2008, the Company reviewed its e-cash operations and determined that certain provisions associated with its commerce based transactions should not be recorded, and further that, based on new facts and circumstances, certain estimates should be revised. Accordingly, approximately \$1,700 that was recorded as a liability for future payments was no longer required. (2008: \$1,200) These changes were recorded in revenue in the accompanying statements of (loss)/earnings and comprehensive (loss)/income.

### (q) Long-lived assets:

Long-lived assets comprise capital assets and intangible assets and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset or groups of assets and its eventual disposition. Measurement of any impairment loss for long-lived assets is based on the amount by which the carrying value exceeds the fair value of the asset. See notes 4 and 6 for discussions of the impairments.

# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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## 1. Significant accounting policies (continued):

(r) Recent accounting pronouncements:

International Financial Reporting Standards ("IFRS")

In February 2008, the Accounting Standards Board ("AcSB") confirmed that the use of IFRS will be required in 2011 for publicly accountable enterprises in Canada. In April 2008, the AcSB issued an IFRS Omnibus Exposure Draft proposing that publicly accountable enterprises be required to apply IFRS, in full and without modification, on January 1, 2011.

In June 2008, the Canadian Securities Administrators ("CSA") issued Staff Notice 52-321, Early Adoption of IFRS which indicated that the CSA would be prepared to grant an exemption to allow Canadian financial statement issuers to adopt IFRS early on a case-by-case basis, provided that they could demonstrate that they met certain conditions.

The adoption of IFRS will require the restatement of amounts reported by the Company for its previous year ended, and of the opening balance sheet as at the date of adoption.

The Company intends to adopt IFRS for the accounting period commencing January 1, 2011 and is continuing to assess the financial reporting impacts of the adoption of IFRS. The Company expects financial reporting impacts to deferred tax, intangible assets and share based payments. However, the impact on future financial position and results of operations is not reasonably determinable or estimable at this time. The Company does anticipate a significant increase in disclosure resulting from the adoption of IFRS and is continuing to assess the level of disclosure required.

The IFRS conversion project consists of three phases: Scoping and Diagnostics, Analysis and Development and Implementation and Review.

Phase One: Scoping and Diagnostics, which involved project planning and staffing and identification of differences between current Canadian GAAP and IFRS, has been completed.

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# CRYPTOLOGIC LIMITED

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## **1. Significant accounting policies (continued):**

Phase Two: Analysis and Development, involves detailed diagnostics and evaluation of the financial impacts of various options and alternative methodologies provided for under IFRS; identification and design of operational and financial business processes; initial staff and audit committee training; analysis of IFRS 1 optional exemptions and mandatory exceptions to the general requirement for full retrospective application upon transition to IFRS; summarization of 2011 IFRS disclosure requirements; and development of required solutions to address identified issues. Phase Two is underway, but has not yet been completed and has not yet identified any significant financial statement impacts.

Phase Three: Implementation and Review will involve the execution of changes to information systems and business processes; completion of formal authorization processes to approve recommended accounting policy changes; and further training programs across the Company's finance and other affected areas, as necessary. It will culminate in the collection of financial information necessary to compile IFRS-compliant financial statements and reconciliations; embedding of IFRS in business processes; and audit committee approval of IFRS-compliant financial statements.

## **2. Security deposits and restricted cash:**

Security deposits are amounts held by the Company's bank as collateral provided to payment processors that process deposits and credit card transactions.

At December 31, 2009, the Company has no restricted cash. At December 31, 2008 restricted cash comprised a required deposit of \$5,000 to support a letter of credit to the Lottery Gaming Authority of Malta ("LGA") to support user funds on deposit. In July 2009 the LGA agreed that the \$5,000 letter of credit was no longer required and the letter was returned to the Company. Under a revised arrangement with the LGA, the Company is required to maintain funds in a designated bank account which, at all times, are not less than user funds held on deposit. At December 31, 2008, restricted cash also included \$2,175, held in escrow, that would have been paid to the Company's former CEO had there been a change in control of the company prior to April 30, 2009. As there was no change in control of the Company, no amounts were paid and the restriction has expired.

## **3. User funds held on deposit:**

User funds held on deposit represent amounts deposited by end users of licensees for playing online games. These funds are treated as deposits of the end users until such games are played.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**4. Capital assets:**

	<b>Computer equipment</b>	<b>Office furniture and licenses</b>	<b>Computer software development</b>	<b>Capitalized software improvements</b>	<b>Leasehold improvements</b>	<b>Total</b>
<b>Cost</b>						
Balance, January 1, 2009	\$ 13,175	\$ 2,084	\$ 10,239	\$ 8,300	\$ 5,807	\$ 39,605
Additions	67	78	80		220	445
Disposals		(59)				(59)
Impairments	(7,869)	(1,090)		(3,552)	(3,463)	(15,974)
SRED rebate				(448)		(448)
Balance, December 31, 2009	5,373	1,013	10,319	4,300	2,564	23,569
<b>Amortization</b>						
Balance, January 1, 2009	(9,795)	(1,274)	(8,490)		(1,343)	(20,902)
Charge for the year	(1,350)	(168)	(1,181)	(862)	(652)	(4,213)
Impairments	6,645	791		862	966	9,264
Amortization on disposals		56				56
Balance, December 31, 2009	(4,500)	(595)	(9,671)		(1,029)	(15,795)
<b>Net book value</b>						
Balance, December 31, 2009	\$ 873	\$ 418	\$ 648	\$ 4,300	\$ 1,535	\$ 7,774
Balance, December 31, 2008	\$ 3,380	\$ 810	\$ 1,749	\$ 8,300	\$ 4,464	\$ 18,703

Amortization expense of capital assets during the year was \$4,216 (2008: \$4,306; 2007: \$5,361). During 2009 and 2008, there were no changes in the estimated useful lives of computer equipment and office furniture and equipment.

During 2009, as part of the Company's reorganization plan, the Company implemented a number of cost saving measures including a data centre rationalization, reducing the number of data centres from eleven to five, consolidating the number of servers in use and performing a comprehensive review of surplus computer and office furniture and equipment arising out of employee terminations. As a result of this review the Company determined that certain assets were impaired and accordingly recorded an impairment charge to computer equipment and office equipment of \$1,224 and \$299 respectively. In addition, in December 2009, the Company opted to exercise its right to early termination of one of its leased properties. See note 13 for further discussion. The Company determined that the leasehold improvements associated with the property were impaired and accordingly recorded an impairment charge of \$2,497. All amounts have been recorded in the consolidated statements of (loss)/earnings and other comprehensive (loss)/income.

# CRYPTOLOGIC LIMITED

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#### **4. Capital assets (continued):**

During 2009, as a result of difficult macroeconomic conditions and a decline in expected future revenues, the Company performed an impairment review on software development projects associated with the software gaming platform (“Agile”) designed to support multiple gaming methods. The Company completed a valuation of these capitalized software development costs using the relief-from-royalty method which includes estimating the net cash flows expected from these projects and discounting these cash flows to present value at a discount rate that considers the degree of risk or uncertainty associated with the realization of the estimated net cash flows.

Using this approach, the Company determined that the carrying amounts of these assets exceeded their fair value. Consequently, the Company recorded an impairment loss of \$2,690, the amount by which the carrying value exceeded the estimated fair value. This impairment loss is included in asset impairments in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/income. Once these assets are put into use, the Company will commence amortization on a straight line basis over seven years. The Company had previously expected a five year useful life for these assets.

During 2008, the Company completed a valuation of Agile using a similar relief from royalty method as the scalable server infrastructure was taking longer and costing more to complete than expected. As a result the company recorded an impairment loss of \$6,680, the amount by which the carrying value exceeded the estimated fair value. This impairment loss was included in asset impairments in the accompanying consolidated statements of (loss)/earnings and other comprehensive (loss)/income.

The Company benefits from a Canada tax incentive program (“SRED”) designed to encourage businesses operating within Canada developing advanced technological products and processes. The tax credit was based on work capitalized as part of the Agile software development project therefore the Company reduced the cost basis of Agile by \$448, the net amount to be paid to the Company.

In 2008, the Company also recorded a loss of \$427 in relation to software development projects associated with integration of certain poker operations. Refer to note 15 for details.

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Notes to Consolidated Financial Statements (continued)

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## 5. Long-term investments:

In June 2007, the Company acquired a 19.4% ownership interest in 568 Network Inc. ("568 Inc."), a privately held company, for \$1,068. 568 Inc. is a developer and distributor of online casual games to the Chinese market. During 2008, the Company made a further investment by way of a \$350 loan. This loan is convertible into preference shares at the option of the Company. The investment and the loan are classified as available-for-sale. The Company has determined that the convertible feature of this loan is an embedded derivative, which is immaterial.

During the year various indicators of impairment were identified including significant financial difficulty and continued operating losses. The Company reviewed this investment for impairment by performing a discounted net cash flow on data not readily available in the market including, but not limited, to future expected net cash flows from this business. As a result of this analysis, the Company determined that the carrying value exceeded the fair value and these declines in value were other than temporary. The Company recorded an impairment charge of \$1,418 or the entire carrying value of the investment, which is included in asset impairments in the accompanying statements of net (loss)/earnings and comprehensive (loss)/ income.

In November 2007, the Company acquired a 12.7% ownership interest in Mikoishi (Asia Pacific) Pte Ltd. ("Mikoishi"), a privately held company, for cash consideration of \$4,258. Mikoishi is a developer and marketer of gaming products for the mobile computing markets and is located in Singapore. The investment in Mikoishi is designated as available-for-sale which is measured at fair value. In June 2009, the Company made a further investment by way of a \$277 loan. This loan is convertible into preference shares at the option of the Company. The investment and the loan are classified as available-for-sale. The Company has determined that the convertible feature of this loan is an embedded derivative, which is immaterial.

During the year various indicators of impairment were identified including significant financial difficulty, restructuring activities and continued operating losses. The Company reviewed this investment for impairment by performing a discounted net cash flow on data not readily available in the market including, but not limited to, future expected net cash flows from this business. As a result of this analysis, the Company determined that the carrying value exceeded the fair value and these declines in value were other than temporary. Accordingly, the company recorded an impairment charge of \$2,335 or the entire remaining carrying value of the investment, which is included in asset impairments in the accompanying statements of net (loss)/earnings and comprehensive (loss)/ income. In 2008, the Company received evidence of Mikoishi's current fair value and as a result, the Company had recorded a write down in the value of the investment of \$2,200, which is included in asset impairments in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/income.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## 5. Long-term investments (continued):

In March 2008, the Company acquired a 15.0% ownership interest in Mobilebus Inc. (“Mobilebus”), a privately held Korean company specializing in game development, for cash consideration of \$645. In exchange for cash consideration, the Company received common shares. The investment in Mobilebus is classified as available-for-sale.

During the year various indicators of impairment were identified including significant financial difficulty, declining revenues and difficult macroeconomic conditions. The Company reviewed this investment for impairment by performing a discounted net cash flow on data not readily available in the market including, but not limited to, future expected net cash flows from this business. As a result of this analysis, the Company determined that the carrying value exceeded the fair value and these declines in value were other than temporary. The Company recorded an impairment charge of \$645 or the entire carrying value of the investment, which is included in asset impairments in the accompanying statements of net (loss)/earnings and comprehensive (loss)/ income.

In May 2008, the Company acquired an 11.1% interest in Jingle Prize Inc. (“Jingle”), a leading supplier of online mahjong games, for \$1,000. In exchange for the cash consideration, the Company received preference shares, which rank pari passu with the common shares of Jingle with respect to all dividends and voting rights. The terms of this agreement require the Company to make additional investments in Jingle if certain performance criteria are met. In December 2008, the first performance criteria were met resulting in an additional investment of \$700, increasing the Company’s equity ownership in Jingle to 18.9%. During the first quarter of 2009, the Company made a further investment by way of a \$200 loan. This loan is convertible into preference shares at the option of the Company. The investment and the loan are classified as available-for-sale. The Company has determined that the convertible feature of this loan is an embedded derivative, which is immaterial.

During the year various indicators of impairment were identified including significant financial difficulty, continued operating losses and significantly reduced operations. The Company reviewed this investment for impairment by performing a discounted net cash flow on data not readily available in the market including, but not limited to, future expected net cash flows from this business. As a result of this analysis, the Company determined that the carrying value exceeded the fair value and these declines in value were other than temporary. Accordingly, the Company recorded an impairment charge of \$1,900 or the entire carrying value of the investment, which is included in asset impairments in the accompanying statements of net (loss)/earnings and comprehensive (loss)/ income.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**5. Long-term investments (continued):**

The fair value measurements recorded above were computed using data that is not observable in the market and therefore classified as Level 3 under Section 3862. A summary of the fair value measurements follows:

	<b>Long-term investments</b>	
Balance, December 31, 2007	\$	5,326
Investments		2,695
Impairments recorded		(2,200)
Balance, December 31, 2008		5,821
Investments		477
Impairments recorded		(6,298)
Balance at December 31, 2009	\$	33,916

**6. Goodwill and intangible assets:**

In January 2007, the Company acquired the poker brand and the customer list of Parbet.com. The total cash consideration paid was \$11,770, with \$11,746 allocated to the brand and \$1,332 allocated to the customer list. The Company also recorded a future income tax liability of \$1,308.

In 2008, due to decreasing poker revenues and reduced expectations of the Parbet.com brand, the Company reviewed the intangible assets for impairment. The Company completed a valuation of the intangible assets using the relief-from-royalty method, using probability weighted net cash flows expected from Parbet.com and discounting these cash flows to present value at a discount rate that considers the degree of risk or uncertainty associated with the realization of the estimated net revenues. Using this approach, the Company determined that the carrying amounts of the intangible assets exceeded their fair value and recorded an impairment loss of approximately \$7,214. The impairment loss included a \$10,592 reduction in the cost basis of the intangibles as well as \$2,439 of accumulated amortization and a \$939 reduction in the deferred tax liability. The impairment loss is included in the asset impairments in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/income for the year ended December 31, 2008.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## **6. Goodwill and intangible assets (continued):**

The brand is being amortized over 12 years and the customer list over 5 years. During the year, the Company recorded \$297 of amortization associated with the intangible assets (2008: \$1,246, 2007: \$1,042). At December 31, 2009, accumulated amortization associated with brand and the customer list was \$227 and \$70, respectively (2008: nil).

In August 2007, the Company acquired 100% of the assets and operations of Casino.co.uk, a gaming portal, for a purchase price of \$6,098, including \$182 related to the costs of acquisition. The Company has included the results of these operations in its consolidated results of operations since the date of acquisition. The acquisition is accounted for as a business combination using the purchase method of accounting. During 2008, the Company paid \$1,254 of additional consideration to the seller as a result of Casino.co.uk meeting certain performance criteria. This additional consideration was recorded as an increase to goodwill. Including the amounts recorded in 2008, the Company has allocated \$1,323 of the purchase price to the brand name, \$1,630 to the customer list and \$4,769 to goodwill. The Company also recorded a future income tax liability of \$370. The brand name and the customer list are being amortized over their estimated useful lives of 12 years and 7 years, respectively. During the year, the Company recorded \$343 of amortization associated with the intangible assets (2008: \$342, 2007: \$115). At December 31, 2009, the accumulated amortization associated with the customer list and the brand was \$543 and \$257 respectively (2008: \$310 and \$147).

Goodwill is not amortized and is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. During the year, the results of the portals business were below expectations and the market capitalization of the Company was significantly lower than the Company's net assets, which were both indications that the value of the goodwill associated with the portal business was impaired. The implied fair value of the goodwill was determined by discounting expected net future cash flows of the portals business. As a result, the Company decided that the carrying value of the goodwill exceeded its fair value and recorded an impairment charge of \$6,545, its entire value. The impairment loss is included in impairment of goodwill in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/income.

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# CRYPTOLOGIC LIMITED

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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## 7. Minority interest:

As described in the preamble to the notes, pursuant to a business reorganization implemented by way of the Arrangement and approved by the shareholders on May 24, 2007, the Company acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement became an indirect subsidiary of the Company. As part of the Arrangement, taxable Canadian residents received exchangeable shares of CEC, an indirect subsidiary of CryptoLogic Limited. The CEC shares are, as nearly as practicable, the economic equivalent of CryptoLogic Limited shares. As a result of the Arrangement, a total of 12.6 million and 1.3 million shares of the Company and CEC were issued, respectively.

The shares issued by CEC are considered a non-controlling interest of the Company for accounting purposes and, consequently, a proportional amount of the Company's shareholders' equity was recorded separately as minority interest on the consolidated balance sheets. Accordingly, on June 1, 2007, minority interest of \$10,800 was recorded in the consolidated balance sheet. In previous years, a similar proportional share of the net (losses)/earnings associated with subsidiaries directly or indirectly owned by CEC was included in the consolidated statements of (loss)/earnings and comprehensive (loss)/income as minority interest.

During the year, the Company reviewed the key terms associated with ownership of a CEC share and changed its accounting policy for computing the proportional share of the net (losses)/earnings associated to CEC shareholders. The Company will no longer differentiate between companies directly or indirectly owned by CEC and those that are not. Consequently, minority interest will be calculated as a proportional share of the net (losses)/earnings of the consolidated company. This change in accounting policy increased the loss attributable to CEC shareholders by \$1,313. The revised calculation links, more closely, the proportional share of net (losses)/earnings of CEC shareholders to those of non CEC shareholders. The Company has reviewed this change of accounting policy on prior reported periods and concluded that the change in accounting policy would have been immaterial. Earnings per share is not impacted by this change. The Company calculates minority interest under Handbook Section 1600, Consolidated Financial Statements.

In addition, dividends paid to CEC shareholders reduce minority interest on the consolidated balance sheets. For accounting purposes, when CEC shares are exchanged, the proportional share of the minority interest recorded on the consolidated balance sheet is reduced and share capital increased based on the pro-rata number of shares exchanged to the total number of CEC shares outstanding. Since June 1, 2007, a total of 307,200 CEC shares have been exchanged for the Company's shares.

# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

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## **8. Capital risk management:**

The Company defines capital as its shareholders' equity and has a policy to maintain a strong capital base so as to maintain investor and market confidence and to sustain future development of the business. The Company is listed on three major exchanges, the Toronto Stock Exchange, NASDAQ and London Stock Exchange. The Company monitors both the demographic spread of shareholders, as well as the return on equity.

At December 31, 2009 the Company had \$36,796 (December 31, 2008: \$72,440) shareholders' equity. The Company's capital gives it the financial flexibility to take advantage of opportunities in its markets and consider potential strategic acquisitions. Historically, the Company has also used its shareholders' equity to pay dividends and repurchase shares under its normal course issuer bid.

The Company offers stock options to key employees and directors. At December 31, 2009 employees and directors held 563,521 options to purchase common shares of the Company.

On November 13, 2009, a dividend of \$0.01 per share was announced, a decrease from \$0.03 per share announced after the first and second quarter in 2009. While the Company does not expect to declare any dividends in the short term, each future quarterly dividend will be subject to Board approval based on the Company's financial results.

In November 2007, the Company filed a Normal Course Issuer Bid (the "2008 Normal Course Issuer Bid") that entitled the Company to acquire and cancel up to 1,281,000 of its common shares between November 14, 2007 and November 13, 2008. All purchases were to be made on the open market at the market price at the time of the purchase. For the year ended December 31, 2008, the Company repurchased 124,905 shares, for a total cost of \$1,420 associated with the 2008 Normal Course Issuer Bid.

In November 2008, the Company filed a Normal Course Issuer Bid (the "2009 Normal Course Issuer Bid"), which authorized the Company to acquire and cancel up to 1,267,871 of its common shares between December 3, 2008 and December 2, 2009. At December 31, 2009, there were no purchases under the 2009 Normal Course Issuer Bid.

There were no changes in the Company's policy for managing capital during the year ended December 31, 2009. Neither the Company, nor any of its subsidiaries, is subject to externally imposed capital requirements.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

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**9. Share capital:**

Authorized:

Unlimited common shares with no par value

Issued and outstanding:

	Issued common shares		Contributed	Total
	Shares	Amount	surplus	
(in thousands)				
Balance, December 31, 2007	12,813	\$ 33,339	\$ 68	\$ 33,407
Shares exchanged (a)	24	198		198
Common shares repurchased	(125)	(327)		(327)
Exercise of stock options	15	274		274
Balance, December 31, 2008	12,727	33,484	68	33,552
Shares exchanged (a)	66	364		364
Balance at December 31, 2009	12,793	\$ 33,848	\$ 68	\$ 33,916

- (a) The Company acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement became an indirect wholly- owned subsidiary of CryptoLogic Limited. As consideration for the acquisition, CryptoLogic Limited issued either an equivalent amount of its common shares or, in the case of taxable Canadian residents, exchangeable shares of CEC, an indirect subsidiary of the Company. The CEC shares can be exchanged by the holders for an equal number of CryptoLogic Limited common shares at any time. These CEC shares have all the economic and voting rights of CryptoLogic Limited shares.

As a result of the reorganization, a total of 12.6 million and 1.3 million shares of CryptoLogic Limited and CEC were issued, respectively. Since then, a total of 307,200 shares of CEC have been exchanged, with the remaining shares of CEC being reflected as minority interest as at December 31, 2009.

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**CRYPTOLOGIC LIMITED**

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**9. Share capital (continued):**

On June 1, 2014, the Company will redeem all but not less than all of the then outstanding CEC shares for an amount per share equal to the redemption price, which amount will be satisfied through the issuance and delivery of one CryptoLogic Limited common share for each CEC share. CryptoLogic Limited has issued a special voting share to a third party trustee, the purpose of which is to provide holders of CEC shares with the right to vote on the Company's matters. This share has been recorded in the share capital of the accompanying consolidated balance sheet at December 31, 2009.

## (b) Normal course issuer bid:

During 2009, 2008 and 2007 under normal course issuer bids, the Board of Directors approved the repurchase and cancellation of up to the following number of shares, representing 10% of the outstanding common shares at that time:

Normal course issuer bid	Authorized shares	Repurchased and cancelled shares		
		2009	2008	2007
November 14, 2007 to November 13, 2008	1,281,000		124,905	
December 3, 2008 to December 2, 2009	1,267,871			

In November 2007, the Board of Directors approved the renewal of the above share purchase plan, under a normal course issuer bid, to repurchase and cancel up to 1,281,000 of the Company's outstanding common shares for the period commencing November 14, 2007 and ending November 13, 2008. CryptoLogic Limited repurchased and cancelled 124,905 common shares during 2008 for a total cost of \$1,420 of which \$1,093, representing the excess of purchase price over stated value, was charged to retained earnings.

In November 2008, the Board of Directors authorized the Company to purchase up to 1,267,871 shares of the issued ordinary shares on the open market through facilities of the Toronto Stock Exchange. Purchases under the 2009 Normal Course Issuer Bid could have potentially commenced on December 3, 2008 and terminated on December 2, 2009. In 2009, the Company did not purchase any shares under the Normal Course Issuer Bid.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**10. Stock-based compensation and employee benefits:**

## (a) Stock option plan:

Under the stock option plan, the Company may grant options to directors, officers and other key employees to purchase common shares. All outstanding options of CryptoLogic Inc. as of the date of Arrangement were fully assumed by CryptoLogic Limited under the same terms and conditions as originally granted by CryptoLogic Inc. Under the plan, a maximum of 3,900,000 common shares may be issued. The exercise price of the options may not be less than the market value of the underlying common shares on the date of grant. The Company generally grants stock options with an exercise price at the closing price on the date of grant. There are 916,691 (2008: 385,001; 2007: 109,412) common shares available to be issued under the stock option plan as at December 31, 2009. Options typically vest over a period of three or four years, as determined at the date of grant, and the term of the options may not exceed five years.

Details of stock option transactions are as follows:

	2009		2008		2007	
	Number of options	Weighted average exercise price of options	Number of options	Weighted average exercise price of options	Number of options	Weighted average exercise price of options
		(Cdn.\$)		(Cdn.\$)		(Cdn.\$)
Options outstanding, beginning of year	1,095,211	23.88	1,391,525	24.65	1,006,584	21.35
Granted	25,000	4.46	145,000	18.68	896,500	26.35
Exercised			(15,725)	12.16	(286,997)	15.71
Forfeited	(556,690)	25.02	(425,589)	26.62	(224,562)	25.16
Options outstanding, end of year	563,521	21.89	1,095,211	23.88	1,391,525	25.13
Options exercisable, end of year	326,452	23.59	566,189	25.45	331,894	24.65

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**10. Stock-based compensation and employee benefits (continued):**

Range of exercise price	2009			2009		
	Number outstanding	Options outstanding	Weighted average exercise price	Options exercisable	Number exercisable	Weighted average exercise price
		Weighted average remaining life (years)				
(Cdn \$)			(Cdn \$)			(Cdn \$)
\$0.01-\$5.00	15,000	4.61	3.24	1,250		3.12
\$5.01-\$15.00	10,000	4.49	6.30			
\$15.01-\$20.00	225,500	3.17	18.78	79,000		18.72
\$20.01-\$25.00	179,271	1.27	23.60	150,077		23.56
\$25.01-\$30.00	130,750	1.39	28.02	93,125		27.82
\$30.01-\$35.00	3,000	0.13	30.85	3,000		30.85
	563,521	2.20	21.89	326,452		23.59

The Company expenses the cost of all stock option grants issued on or after January 1, 2003, determined using the fair value method. The estimated fair value of the options is recorded over the periods that the options vest. The fair value of options granted were estimated using the Black-Scholes option pricing model with the following weighted average assumptions:

	<b>2009</b>	<b>2008</b>	<b>2007</b>
Dividend yield	6.17%	2.12%	1.90%
Risk-free interest rate	1.30%	2.77%	4.07%
Expected volatility	65.00%	46.12%	52.0%
Expected life of options in year	3	3	3

The weighted average fair value of options granted during 2009 was \$1.54 (2008: \$5.37; 2007: \$7.89).

Included in operating costs is the cost of stock options in the amount of \$777 (2008: \$1,895; 2007: \$2,732). Included in reorganization costs is the cost of stock options in the amount of nil (2008: nil; 2007: \$982).

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**10. Stock-based compensation and employee benefits (continued):**

## (b) Long-term incentive plan:

During the year, the Company recorded an expense of \$26 associated with its long term incentive plans. In 2008 the Company recorded a net benefit of \$452 in operating expense as the Company determined that the probability of achieving the targets of the 2007 plan were remote. The Company recorded an expense of \$155 in 2007.

## (c) Defined contribution pension scheme:

The Company contributes to a defined contribution pension plan for a limited number of employees. During 2009 and 2008 the amount charged to the statements of (loss)/earnings and comprehensive (loss)/income and the amount outstanding at year end were immaterial (2007: nil).

**11. Commitments and contingencies:**

- (a) The Company has operating lease agreements for premises expiring at various periods up to September 2013. The future minimum annual rental payments on the operating leases are as follows:

2010	\$ 1,661
2011	658
2012	660
2013	331

- (b) The Company has sublease agreements for certain of its premises located in Toronto. As a result of the Company exercising its right to exit the premises future sublease revenues of only \$110 will be realized in 2010.

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**CRYPTOLOGIC LIMITED**

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**11. Commitments and contingencies (continued):**

- (c) The Company has guaranteed minimum payments and purchase commitments for certain intellectual property rights up to 2014:

2010	\$	6,096
2011	\$	2,621
2012	\$	554
2013	\$	225
2014	\$	25

- (d) In December 2009, in accordance with the rental agreement, the Company exercised its right to exit the leasehold premises in Toronto and recorded termination costs of \$1,764 payable on termination in July 2010. The termination costs are included in reorganization costs in the accompanying statements of net (loss)/earnings and comprehensive (loss)/income.
- (e) The Company and its subsidiaries are involved in certain claims and litigation arising out of the ordinary course and conduct of business, including intellectual property matters. Management assesses such claims and, if considered likely to result in material exposure and where the amount of the claim is quantifiable, provisions for loss are made based on management's assessment of the likely outcome. Management does not provide for claims that are considered unlikely to result in a significant loss, claims for which the outcome is not determinable or claims where the amount of the loss cannot be reasonably estimated. Any settlement or awards under such claims are provided for when reasonably determinable. During 2009, the Company determined its accrual of \$750 for certain contingencies was no longer required, increasing revenue by a corresponding amount (2008: \$1,000, 2007: \$2,000).
- (f) During 2009 and 2008, the Company reviewed its e-cash operations and determined that certain provisions associated with its commerce based transactions should not be recorded, and further that, based on new facts and circumstances, certain estimates should be revised. Accordingly, approximately \$1,700 that was recorded as a liability for future payments was no longer required (2008: \$1,200). These changes were recorded in revenue in the accompanying statements of (loss)/earnings and comprehensive (loss)/income.



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Notes to Consolidated Financial Statements (continued)

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**11. Commitments and contingencies (continued):**

- (g) During the fourth quarter of 2009, the Company performed an analysis of the accumulation of the funds in the jackpot provision and a statistical analysis of the amounts required to address jackpot payouts and resets. The Company revised its estimated liability based on this analysis. This change of estimate resulted in the reduction of the liability for jackpot accrual and a corresponding increase in revenue of \$841. The accrual for the jackpot at the consolidated balance sheet dates is included in accounts payable and accrued liabilities. At December 31, 2009, accounts payable and accrued liabilities include \$3,020 in jackpot provisions (2008: \$3,152). This amount is sufficient to cover the full amount of any required pay-out.

**12. (Loss)/earnings per common share:**

(Loss)/earnings per share are calculated using the two-class method, whereby common shares of the Company and the fully participating exchangeable common shares of CEC are used to determine the weighted average number of shares outstanding for both basic and diluted (loss)/earnings per share.

The (loss)/earnings attributable to the common shares in calculating the basic and diluted (loss)/earnings per share are as follows:

	2009	2008	2007
(Loss)/earnings attributable to common shares	\$ (35,510)	\$ (32,738)	\$ 5,528
(Loss)/earnings attributable to CEC shares	(2,963)	(2,676)	971
(Loss)/earnings before minority interest	\$ (38,473)	\$ (35,414)	\$ 6,499

The denominator used in calculating basic and diluted (loss)/earnings per common share is calculated as follows:

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<b>All share amounts below are in thousands of shares ( 000s)</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
Weighted average number of common shares outstanding - basic	12,749	12,780	13,223
Add weighted average impact of CEC issued during reorganization	1,071	1,108	668
Total weighted average number of shares outstanding - basic	13,820	13,888	13,891
Add dilutive options			16
Total weighted average number of shares outstanding - diluted	13,820	13,888	13,907

**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**12. (Loss)/earnings per common share (continued):**

Basic and diluted (loss)/earnings per common share are as follows:

	2009	2008	2007
(Loss)/earnings per common share:			
Basic	\$ (2.78)	\$ (2.55)	\$ 0.47
Diluted	\$ (2.78)	\$ (2.55)	\$ 0.47

For the years ended December 31, 2009 and December 31, 2008, basic and diluted net loss per share has been computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period. For the year ended December 31, 2009, diluted net loss per share does not include the effect of the 563,521 (2008: 1,095,211) options to purchase common shares as their impact would be anti-dilutive. For the year ended December 31, 2007, options to purchase 755,971 common shares were excluded from the computation of diluted earnings per share as the exercise price exceeded the average market price of common shares for the reporting year.

**13. Reorganization:**

In November 2008, the Company announced a plan for reorganization of its business after completing a comprehensive review. As a result of that review, the Company decided to reduce costs by outsourcing non core activities, including integrating its poker network with one of the world's leading gaming technology and services companies, transitioning certain functions to lower cost jurisdiction and eliminating certain redundant functions. In December 2009, the Company expanded its reorganization plan due to continued unfavourable macroeconomic

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conditions and will outsource additional technology infrastructure activities, consolidate more of its data centre operations and, migrate additional functions to lower cost jurisdictions resulting in further reduction in headcount and a reduction of its leased office space in both Canada and Cyprus.

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**13. Reorganization (continued):**

The following is a summary of the Company's reorganization plan:

**2008 reorganization charges comprise:**

Consultant fees	\$	499
Employee severance		891
Total 2008 reorganization charges:	\$	1,390

**2009 reorganization charges comprise:**

Consultant fees	\$	1,053
Employee severance		1,146
Lease termination costs		1,764
Asset impairments		3,148
Total 2009 reorganization charges	\$	7,111

The following is a summary of the reorganization accrual:

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Total reorganization charges incurred in 2008 and 2009	\$ 8,501
Total reorganization payments from inception to December 31, 2009 (2008: \$732)	(2,429)
Asset impairments	(3,148)
Included in accounts payable and accrued liabilities at December 31, 2009	\$ 2,924

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The Company expects reorganization expenses to require an outlay of cash of approximately \$5,501, of which \$1,600 of consultant fees and \$900 of employee severance have already been paid as of December 31, 2009. The plan requires an additional cash outlay of \$2,924 consisting primarily of lease termination costs of \$1,764 and employee severance.

**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**14. Departure costs for former CEO:**

In the year ended December 31, 2009 there were no severance costs associated with the former President and CEO.

In February 2008 the Company replaced its former President and CEO. As a result of these changes the Company incurred and paid the following costs in relation to the departure in the year ended December 31, 2008:

Departure	\$	2,877
Profession		523
	\$	3,400

In addition to the above and as part of the arrangements agreed, the former CEO would have been entitled to a further payment of \$2,175 in the event that a change of control of the Company before April 30, 2009. This amount was never paid and the entitlement has expired.

**15. Poker room integration costs**

During 2008, the Company announced its plans to migrate certain poker operations to a third party poker network. Accordingly, the Company identified certain assets including software development projects and certain program costs where the integration of the poker room would indicate that the carrying amounts of such assets may not be recoverable. Measurement of any impairment loss for these assets is based on the

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amount by which the carrying value exceeds the fair value of the asset. With the exception of the Parbet intangible assets discussed in note 6, the fair value of these assets was generally zero. Accordingly, the Company recorded a loss equal to the amount that their respective carrying values exceeded their market values including:

Poker-related program costs	\$ 2,534
Poker development projects	427
Other	163
	\$ 3,124

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**16. Income taxes:**

As described in the preamble to the notes, pursuant to a business reorganization implemented by way of the Arrangement and approved by the shareholders on May 24, 2007, the Company acquired control over all of the issued and outstanding common shares of CryptoLogic Inc., an Ontario company, which through the Arrangement became an indirect subsidiary of the Company, a Guernsey company with tax residence in the Republic of Ireland.

The income tax provision differs from the amount which would be obtained by applying the Irish statutory income tax rate to the (loss)/earnings before income taxes. The following explains the major differences:

	2009	2008	2007
(Loss)/earnings before income taxes	\$ (37,390)	\$ (35,898)	\$ 7,492
Income tax (benefit)/expense at statutory rate of 12.50%: (2008: 12.50%; 2007: 22.34%) (a)	\$ (4,674)	\$ (4,487)	\$ 1,674
Increase/(decrease) in income taxes resulting from:			
Differences in effective income tax rates in foreign jurisdictions	1,340	(196)	823
Permanent differences:			
Net (benefit)/cost of foreign exchange gains not subject to tax	(1,421)	2,150	(1,584)
Non-deductible items	2,041	2,043	1,402
Net benefit of matters resolved in the year	(836)	(275)	(1,314)
Increase/(decrease) in valuation allowance	4,470	(153)	178
Other items	163	434	(186)
Income tax expense/(recovery)	\$ 1,083	\$ (484)	\$ 993

- (a) In 2009 and 2008, 12.50% represents the statutory rate for Ireland. The Company moved its headquarters from Canada to Ireland with effect from June 1, 2007; the statutory rate of 22.34% reflects an average of a 36.12% statutory rate in Canada for five months and a 12.50% statutory rate in Ireland for seven months.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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The tax effects of temporary differences that give rise to significant portions of the future income tax assets and future income tax liabilities at December 31, 2009 and 2008 are as follows:

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

**16. Income taxes (continued):**

	<b>2009</b>	<b>2008</b>
Future income tax assets:		
Non-capital income tax loss carryforward	\$ 4,844	\$ 1,760
Long-term incentive plan	3	
Capital items	939	
Leasehold inducements		347
Accrued liabilities	210	89
Other Items	41	
	6,037	2,196
Valuation allowance	(4,488)	(17)
	1,549	2,179
Future income tax liabilities:		
Intangible assets	(384)	(440)
Capital assets		(140)
Unrealized foreign exchange gains		(51)
	(384)	(631)
Net future income tax assets	\$ 1,165	\$ 1,548
Amounts classified as future tax assets	\$ 1,549	\$ 1,930
Amounts classified as future tax liabilities	(384)	(382)
Net future income tax assets	\$ 1,165	\$ 1,548

The tax losses of the subsidiaries of CryptoLogic Limited that carry forward indefinitely are \$48,117. Although trading losses of these companies can be carried forward indefinitely, a valuation allowance has been recognized against these losses as sufficient profits may not arise in the future to utilize the assets. The tax losses of a Canadian subsidiary are \$356 and carry forward for 20 years.

The Company's federal income tax returns for the years ended December 31, 2003, December 31, 2004, December 31, 2006 and December 31, 2007 are under examination by the Canadian Revenue Agency.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

## **16. Income taxes (continued):**

The Company has a valuation allowance of \$4,488 as of December 31, 2009 to reduce future income tax assets to the amount that is more likely than not to be realized in future periods. In evaluating the Company's ability to recover its future income tax assets, the Company considers all available positive and negative evidence, including operating results, ongoing tax planning and forecasts of future taxable income on a jurisdiction by jurisdiction basis.

The benefit of foreign exchange gains not subject to tax of \$1,421 is primarily a result of recent amendments to Section 261 of the Income Tax Act in Canada that permit certain corporations resident in Canada to elect to determine their Canadian tax amounts in the corporation's "functional currency" as opposed to the general requirement that all amounts that are relevant to the computation of tax under the Canadian Income Tax Act be in Canadian dollars.

## **17. Related party transactions:**

Historically, in the normal course of operations, the Company engaged the services of a law firm in which a member of the Board of Directors is a partner. Fees paid to this firm were \$62 in 2009 (2008: \$420; 2007: \$935) and are included in general and administrative expenses in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/income. At December 31, 2009, there were no amounts outstanding (2008: \$27; 2007: \$85).

The Company paid \$26 (2008: \$15; 2007: \$292) to a second law firm in which a former member of its Board of Directors is a partner. At December 31, 2009, there were no amounts outstanding (2008: nil; 2007: nil).

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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## 18. Financial risk management:

### (a) Overview

The Company has exposure to the following risks from its use of financial instruments.

credit risk

market risk

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits.

Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Company's activities.

### (b) Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its obligations. The carrying amount of the Company's financial assets reflects its expected maximum credit exposure.

#### Accounts Receivable

The Company manages its credit risk associated with accounts receivable by maintaining reserves for potential credit losses. Historically the Company has not experienced any significant credit losses associated with its online poker, casino and Branded Games businesses. The expected growth of Branded Games business and the outsourcing of poker has increased and is expected to increase accounts receivable further as revenue from Branded Games and settlement of player funds between the Company and its poker room operator are collected fifteen days in arrears. Consequently, the Company will have at least one month of Branded Games revenue included in accounts receivable at any balance sheet date. The amount of player funds to be settled between the Company and its poker room operator fluctuates depending on various factors including poker activity and respective skill of players.

The Company has trade accounts receivable and other receivables of \$7,972 (2008: \$6,002). The Company does not have any material accounts receivable balances greater than 90 days outstanding. As a result, the Company believes that its accounts receivable represent a low credit risk and has never recorded a material expense associated with a credit risk exposure.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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## **18. Financial risk management (continued):**

### Cash and Cash Equivalents

The company holds investments, according to Company Investment policy, only in banks carrying an S&P rating of AA/R-1-Mid and higher.

#### **(c) Market Risk**

Market risk is the risk that changes in the market prices such as fluctuations in foreign exchange rates and interest rates, will affect the Company's net earnings or the value of its financial instruments.

#### Currency Risk

The Company operates internationally giving rise to exposure to changes in foreign exchange rates. The currency risk is derived from revenue denominated in currencies other than U.S. dollars, its functional currency, primarily British pounds and euro, and expenses associated with its multinational operations (primarily Canadian dollars, the British pounds and euro) as well as the respective receivable and payable balances. The Company is also exposed to currency risk on cash and cash equivalents and other current assets denominated in foreign currencies. As at December 31, 2009, approximately 78% of the Company's financial assets are denominated in its functional currency.

#### Interest Rate Risk

The Company is exposed to interest rate risk principally on its cash and cash equivalents that generally have maturity dates of less than 90 days. The Company has no interest bearing debt.

The weighted average effective interest rate on the Company's cash and cash equivalents as at December 31, 2009 was 1.24% (2008: 2.53%).

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**18. Financial risk management (continued):****(d) Quantification of risk exposure: foreign currency risk**

At December 31, 2009, the Company's gross balance sheet exposure to foreign currency risk was substantially as follows:

<b>In USD equivalents (000 s)</b>	<b>USD</b>	<b>EURO</b>	<b>GBP</b>	<b>Others</b>	<b>Total</b>
Cash and cash equivalents and user funds	\$ 28,703	\$ 966	\$ 631	\$ 1,076	\$ 31,376
Accounts receivable and other	\$ 2,399	\$ 4,046	\$ 1,392	\$ 135	\$ 7,972
Accounts payable and accrued liabilities	\$ (2,353)	\$ (2,975)	\$ (4,561)	\$ (3,267)	\$ (13,156)
User funds	\$ (3,420)	\$ (3,684)	\$ (825)	\$	\$ (7,929)
Net balance sheet exposure	\$ 25,329	\$ (1,647)	\$ (3,363)	\$ (2,056)	\$ (18,263)

The Company's revenue exposure for revenue denominated in foreign currencies was substantially as follows for the years ended:

<b>In USD equivalents (000 s)</b>	<b>USD</b>	<b>EURO</b>	<b>GBP</b>	<b>CDN</b>	<b>Others</b>	<b>Total</b>
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Revenue:

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2009	\$	13,664	\$	10,400	\$	15,730	\$		\$	39,794		
2008	\$	19,042	\$	12,404	\$	30,080	\$		\$	61,526		
2007	\$	28,672	\$	12,027	\$	32,946	\$	14	\$	73,659		
<u>Expenses:</u>												
2009	\$	23,289	\$	17,648	\$	14,801	\$	21,287	\$	605	\$	77,630
2008	\$	24,536	\$	27,644	\$	18,250	\$	28,344	\$	829	\$	99,603
2007	\$	18,005	\$	6,632	\$	12,069	\$	27,861	\$	7,817	\$	72,384

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# CRYPTOLOGIC LIMITED

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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## **18. Financial risk management (continued):**

### Fair Value Sensitivity Analysis

Gross Balance Sheet Exposure: A 10% strengthening of the U.S. dollar against the currencies in the above table (gross balance sheet exposure) at December 31, 2009 would have decreased net losses by approximately \$707. This analysis assumes that all other variables, in particular interest rates, remain constant and represents the Company's gross balance sheet exposure at December 31, 2009. A 10% weakening of the U.S. dollar against the same would have had an equal but opposite effect. During the current year, the Company incurred a loss of approximately \$284 on the revaluation of its net balance sheet exposure. This loss was caused by the depreciation of the British pound and euro in comparison to the U.S. dollar, at a time when the Company had significant net assets in each of these currencies.

Net Revenue Exposure: A 10% strengthening on average of the U.S. dollar against the currencies in the above table for the year ended December 31, 2009 would have decreased net revenue by approximately \$2,613. This analysis assumes that all other variables, in particular interest rates, remained constant during the year and represents the exposure of the Company's revenues denominated in foreign currencies, to the relative strength of its functional currency. A 10% weakening of the U.S. dollar against the same would have had an equal but opposite effect.

Expense Exposure: A 10% strengthening on average of the U.S. dollar against the currencies in the above table for the year ended December 31, 2009 would have decreased expense, and correspondingly decreased net losses, by approximately \$5,434. This analysis assumes that all other variables, in particular interest rates, remained constant during the year, and represents the exposure of the Company's expenses denominated in foreign currencies to the relative strength of its functional currency. A 10% weakening of the U.S. dollar against the same would have had an equal but opposite effect.

Quantification of risk exposure: The Company is exposed to interest rate risk principally on its cash deposits and short-term money market investments of generally less than 90 days. The exposure is principally to a decrease in interest rates in the United States, Britain and the Eurozone.

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**CRYPTOLOGIC LIMITED**

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**18. Financial risk management (continued):**

Interest Income Exposure: A 100 basis point increase in interest rates on average for the year ended December 31, 2009 would have increased interest income by approximately \$357. This analysis assumes that all other variables remained constant during the quarter. A 100 basis point decrease in interest rates on average would have had an equal but opposite effect.

**Foreign Exchange**

In 2009, the Company recognized a total foreign exchange loss of \$284 (2008: foreign exchange loss \$6,151, 2007: foreign exchange gain \$682), which is recorded in operating expenses in the accompanying consolidated statements of (loss)/earnings and comprehensive (loss)/income.

**19. Revenue:**

The Company provides a comprehensive solution including software, network operations, administrative and marketing consulting services to licensed gaming operators that allows licensees to provide online casino and poker games as well as licensees of Branded games and considers these activities to be one reportable segment. Revenue from these offerings for online casino and poker games in 2009 was \$29,951 (2008: \$41,829; 2007: \$49,457) and \$3,516 (2008: \$13,760; 2007: \$19,523), respectively. Revenue from Branded Games activity in 2009 was \$2,813 (2008: \$321; 2007: nil). In 2008, this revenue category was combined with casino revenue. Revenue from other sources was \$3,514 (2008: \$5,616; 2007: \$4,679).

**20. Components of non-operating income:**

Non operating income comprises gains recorded on the sale of common shares acquired and sold in a specific business endeavour as well as certain foreign exchange gains recorded on cash deposits earmarked for additional share purchases. These gains are offset, in part, by related expenses.

	2009	2008	2007
Gain on temporary holding in shares	\$	\$ 801	\$
Foreign exchange gain and interest on temporary cash deposit		544	
Related expenses		(1,243)	
Non operating income	\$	\$ 102	\$

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**CRYPTOLOGIC LIMITED**

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

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**21. Differences between Canadian and United States generally accepted accounting principles:**

The significant measurement differences between Canadian and U.S. GAAP affecting the consolidated financial statements, as noted above, are as follows:

	2009	2008	2007
(Loss)/earnings based on Canadian GAAP	\$ (35,510)	\$ (32,738)	\$ 5,528
Adjustment for stock-based compensation (a)	(1,159)	(310)	112
(Loss)/earnings based on U.S. GAAP	\$ (36,669)	\$ (33,048)	\$ 5,640

	2009	2008	2007
(Loss)/earnings per common share based on U.S. GAAP:			
Basic	\$ (2.87)	\$ (2.57)	\$ 0.48
Diluted	\$ (2.87)	\$ (2.57)	\$ 0.48

(a) Share based payments

(i) Stock options:

Under Canadian GAAP, the Company does not estimate forfeitures in determining the expense to be recognized over the service period and forfeitures are accounted for as they occur. U.S. GAAP requires an entity to estimate the number of options for which the requisite service is expected to be rendered.

For 2009 the estimated weighted average forfeiture rate is 79%, resulting in a U.S. GAAP stock-based compensation adjustment of \$1,159 compared with a forfeiture rate of 53% in 2008 and a stock-based compensation adjustment of \$310.

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# CRYPTOLOGIC LIMITED

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Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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## **21. Differences between Canadian and United States generally accepted accounting principles (continued):**

### (ii) Long-term incentive plan:

Under Canadian GAAP, the Company uses an intrinsic value-based method to record compensation expense for liability classified awards. U.S. GAAP requires the use of a fair value-based method, rather than an intrinsic value-based method, to measure and record compensation expense for these awards. In 2009, there was no material expense associated with long-term incentive plans as a result the Company has determined there is no material difference to the financial position, cash flows or results of operation between the intrinsic value and the fair value of the units awarded under its long-term incentive plan.

### (b) Income taxes:

U.S. GAAP requires that the Company recognize in its financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. These requirements became effective for the Company on January 1, 2007, with the cumulative effect of the change in accounting principle, if any, recorded as an adjustment to opening retained earnings. The impact of adopting these requirements did not have a material impact on the Company's financial position, cash flows and results of operations.

### (c) Financial instruments:

Effective January 1, 2007, the Company adopted the new Canadian GAAP reporting standards for financial instruments of Handbook Section 1530, Section 3855, Section 3861 and Section 3251.

As a result, under Canadian GAAP, the Company has classified all cash, cash equivalents, short-term investments and user funds on deposit as held-for-trading assets, which are measured at fair value. Under U.S. GAAP, cash, cash equivalents, short-term investments and user funds on deposit would not be classified as held-for-trading assets. Cash, cash equivalents, and short-term investments are measured at cost plus accrued interest and user funds on deposit are measured at the redemption amount. The Company has determined that there is no material difference between the fair value and the cost plus accrued interest or redemption amounts for these financial assets under U.S. GAAP.

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# CRYPTOLOGIC LIMITED

(FORMERLY CRYPTOLOGIC INC.)

Notes to Consolidated Financial Statements (continued)

(In thousands of U.S. dollars, except per share disclosure and where indicated otherwise)

Years ended December 31, 2009, 2008 and 2007

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**21. Differences between Canadian and United States generally accepted accounting principles (continued):**

Furthermore, under Canadian GAAP the Company has classified long-term investments as available-for-sale, which are measured at fair value. These long-term investments do not satisfy the requirements under U.S. GAAP to be classified as available-for-sale, and therefore, these long-term investments are measured at cost under U.S. GAAP. However, the carrying value of long-term investments would be reviewed under U.S. GAAP for declines in value that are other than temporary by considering factors such as current economic and market conditions and the operating performance of the companies and would record reductions in carrying values when necessary.

Adjustments to the fair value of long-term investments are recorded where the market value is readily available. As discussed in note 5, there were various indicators of impairment associated with its long term investments which initiated a comprehensive review of their respective fair values. In 2009, the Company recorded an impairment of \$6,298. In 2008, the Company recorded an impairment of its investment in Mikoishi of \$2,200. The Company has determined there is no material difference on its financial position, cash flows or results of operations between recording its long-term investments at fair value or at cost, adjusted for other than temporary declines in fair value.

(d) Minority Interest:

Under U.S. GAAP, minority interests of \$2,948 and \$6,382 for the years ended December 31, 2009 and 2008 respectively would be combined with shareholders' equity in the accompanying consolidated balance sheet.

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**SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS**

**Accounts Receivable**

**Allowance for Doubtful Accounts**

Years ended December 31(In US\$)

	<b>Balance at Beginning of Year</b>	<b>Charged to Expenses</b>	<b>Write-Offs Net of Recoveries</b>	<b>Balance at End of Year</b>
2007	11,049		(50)	10,999
2008	10,999	(70,162)	81,161	
2009		(16,422)	16,422	

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