Bridgeline Digital, Inc.
Form 10-K
December 29, 2014
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

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

For the fiscal year ended September 30, 2014

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

For the transition period from ______________ to ______________

Commission File Number 333-139298

Bridgeline Digital, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**52-2263942**
State or Other Jurisdiction of Incorporation	IRS Employer Identification No.

80 Blanchard Road	
Burlington, Massachusetts	**01803**
(Address of Principal Executive Offices)	(Zip Code)

(781) 376-5555
(Registrant's telephone number)

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

Title of each class	Name of exchange on which registered
Common Stock, $0.001 par value per share	The NASDAQ Stock Market, LLC

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

None

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

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

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

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

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

Large accelerated filer	Accelerated filer	Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant was approximately $19,525,963 based on the closing price of $1.01 of the issuer's common stock, par value $.001 per share, as reported by the NASDAQ Stock Market on March 31, 2014.

On December 12, 2014, there were 21,974,529 shares of the registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE: Portions of the definitive proxy statement for our 2014 annual meeting of stockholders, which is to be filed within 120 days after the end of the fiscal year ended September 30, 2014, are incorporated by reference into Part III of this Form 10-K, to the extent described in Part III.

Forward Looking Statement

Statements contained in this Annual Report on Form 10-K that are not based on historical facts are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may be identified by the use of forward-looking terminology such as "should," "could," "may," "will," "expect," "believe," "estimate," "anticipate," "intends," "continue," or similar terms or variations of those terms or the negative of those terms. These statements appear in a number of places in this Form 10-K and include statements regarding the intent, belief or current expectations of Bridgeline Digital, Inc. Forward-looking statements are merely our current predictions of future events. Investors are cautioned that any such forward-looking statements are inherently uncertain, are not guaranties of future performance and involve risks and uncertainties. Actual results may differ materially from our predictions. Important factors that could cause actual results to differ from our predictions include the impact of the weakness in the U.S. and international economies on our business, our inability to manage our future growth effectively or profitably, fluctuations in our revenue and quarterly results, our license renewal rate, the impact of competition and our ability to maintain margins or market share, the limited market for our common stock, the volatility of the market price of our common stock, the ability to maintain our listing on the NASDAQ Capital Market, the ability to raise capital, the performance of our products, our ability to respond to rapidly evolving technology and customer requirements, our ability to protect our proprietary technology, the security of our software, our dependence on our management team and key personnel, our ability to hire and retain future key personnel, or our ability to maintain an effective system of internal controls. Although we have sought to identify the most significant risks to our business, we cannot predict whether, or to what extent, any of such risks may be realized, nor is there any assurance that we have identified all possible issues which we might face. We assume no obligation to update our forward-looking statements to reflect new information or developments. We urge readers to review carefully the risk factors described herein and in the other documents that we file with the Securities and Exchange Commission. You can read these documents at www.sec.gov.

Where we say "we," "us," "our," "Company" or "Bridgeline" or "Bridgeline Digital" we mean Bridgeline Digital, Inc.

PART I

Item 1. Business.

Overview

Bridgeline Digital, The Digital Engagement Company™, enables its customers to maximize the performance of their mission critical websites, intranets, and online stores. Bridgeline's iAPPS® platform deeply integrates Web Content Management, eCommerce, eMarketing, Social Media management, and Web Analytics to help marketers deliver online experiences that attract, engage and convert their customers across all digital channels. Bridgeline's iAPPS platform combined with its digital services assists customers in maximizing on-line revenue, improving customer service and loyalty, enhancing employee knowledge, and reducing operational costs.

In fiscal 2012, Bridgeline Digital announced the release of iAPPSds ("distributed subscription"), a platform that empowers franchise and multi-unit organizations with state-of-the-art web engagement management while providing superior oversight of corporate branding. iAPPSds deeply integrates content management, eCommerce, eMarketing and web analytics and is a self-service web platform that is offered to each authorized franchise or dealer for a monthly subscription fee. In fiscal 2013, we acquired franchise web developer ElementsLocal, expanding Bridgeline Digital's presence in the franchise market place.

The iAPPS platform is delivered through a cloud-based SaaS ("Software as a Service") multi-tenant business model, whose flexible architecture provides customers with state of the art deployment providing maintenance, daily technical operation and support; or via a traditional perpetual licensing business model, in which the iAPPS software resides on a dedicated server in either the customer's facility or Bridgeline's co-managed hosting facility.

The iAPPS Platform is an award-winning application recognized around the globe. Our teams of Microsoft Gold© certified developers have won over 100 industry related awards. In recent years, our iAPPS Content Manager and iAPPS Commerce products were selected as finalists for the 2014, 2013, and 2012 CODiE Awards for Best Content Management Solution and Best Electronic Commerce Solution, globally. In 2014 and 2013, Bridgeline Digital won twenty-five Horizon Interactive Awards for outstanding development of web applications and websites. Also in 2013, the Web Marketing Association sponsored Internet Advertising Competition honored Bridgeline Digital with three awards for iAPPS customer websites and B2B Magazine selected Bridgeline Digital as one of the Top Interactive Technology companies in the United States. KMWorld Magazine Editors selected Bridgeline Digital as one of the 100 Companies That Matter in Knowledge Management and also selected iAPPS as a Trend Setting Product in 2013.

Bridgeline Digital was incorporated under the laws of the State of Delaware on August 28, 2000.

Locations

The Company's corporate office is in Burlington, Massachusetts. The Company maintains regional field offices serving the following geographical locations: Atlanta, GA; Baltimore, MD; Boston, MA; Chicago, IL; Dallas, TX; Denver, CO; New York, NY; San Diego, CA; San Luis Obispo, CA; and Tampa, FL. The Company has one wholly-owned subsidiary, Bridgeline Digital Pvt. Ltd. located in Bangalore, India.

Summary of Fiscal 2014

Financial

Total subscription and perpetual license revenue increased 44% to $5.7 million in fiscal 2014 from $4.0 million in fiscal 2013.

Recurring revenue, which reflects amounts that are contractually due to Bridgeline, increased 33% to $6.9 million in fiscal 2014 from $5.2 million in fiscal 2013.

Total iAPPS related revenue increased 8% to $20.3 million in fiscal 2014 from $18.8 million in fiscal 2013.

Non-iAPPS related revenue decreased 40% in fiscal 2014 compared to fiscal 2013.

Products and Services

Products

Subscription and Perpetual Licenses

Revenue from sales of both on-demand SaaS web tools and perpetual licenses is reported as subscription and perpetual licenses in the accompanying consolidated financial statements.

iAPPS Platform

The iAPPS platform provides a unified common set of shared software modules that are critical to today's mission critical websites, on-line stores, intranets, extranets, and portals. The iAPPS platform empowers companies and developers to create websites, web applications and online stores with advanced business logic, state-of-the-art graphical user interfaces, and improved quality.

The iAPPS platform is a Web Engagement Management (WEM) platform that unifies web content management, web Analytics, eCommerce, social media management and eMarketing capabilities deep within the websites, intranets or online stores in which they reside, enabling customers to enhance and optimize the value of their web properties and better engage their website users. The iAPPS platform significantly enhances WEM and Customer Experience Management (CXM) capabilities.

The iAPPSds platform was built specifically to support the needs of multi-unit organizations and franchises, Bridgeline's cloud-based platform allows companies to execute local marketing plans, follow SEO best practices, drive eCommerce initiatives, and measure results with actionable analytics.

The iAPPS suite of products includes:

iAPPS Content Manager allows non-technical users to create, edit, and publish content via a browser-based interface. The advanced, easy-to-use interface allows businesses to keep content and promotions fresh - whether for a public commercial site or a company intranet. iAPPS Content Manager handles the presentation of content based on a sophisticated indexing and security scheme that includes management of front-end access to online applications. The system provides a robust library functionality to manage permissions, versions and organization of different content types, including multimedia files and images. Administrators are able to easily configure a simple or advanced workflow. The system can accommodate the complexity of larger companies with strict regulatory policies. iAPPS Content Manager is uniquely integrated and unified with iAPPS Analyzer, iAPPS Commerce, and iAPPS Marketier; providing our customers with precise information, accurate results, expansion options, and stronger user adoption.

iAPPS Commerce is an online B2B and B2C eCommerce solution that allows users to maximize and manage all aspects of their domestic and international Commerce initiatives. The customizable dashboard provides customers with a real-time overview of the performance of their online stores, including sales trends, demographics, profit margins, inventory levels, inventory alerts, fulfillment deficiencies, average check out times, potential production issues, and delivery times. iAPPS Commerce also provides backend access to payment and shipping gateways. In combining iAPPS Commerce with iAPPS Analyzer and iAPPS Marketier, our customers can take their Commerce initiatives to an advanced level by personalizing their product offerings, improving their marketing effectiveness, providing value-added services and cross selling additional products. iAPPS Commerce is uniquely integrated and unified with iAPPS Analyzer, iAPPS Content Manager, and iAPPS Marketier; providing our customers with precise information, more accurate results, expansion options, and stronger user adoption.

iAPPS Marketier is a marketing lifecycle management solution that includes customer transaction analysis, email management, surveys and polls, event registration and issue tracking to measure campaign return on investment and client satisfaction. Website content and user profiling is leveraged to deliver targeted campaigns and stronger customer relationships. The email management features provide comprehensive reporting capabilities including success rate, and recipient activity such as click-thrus and opt-outs. iAPPS Marketier integrates with leading Customer Relationship Management (CRM’s) systems such as Salesforce.com and leading ad banner engines such as Google. iAPPS Marketier is uniquely integrated and unified with iAPPS Analyzer, iAPPS Content Manager, and iAPPS Commerce; providing customers with precise information, accurate results, expansion options, and stronger user adoption.

iAPPS Analyzer provides the ability to manage, measure and optimize web properties by recording detailed events and subsequently mine data within a web application for statistical analysis. Our customers have access to information regarding where their visitors are coming from, what content and products their viewers are most interested in, and how they navigate through a particular web application. Through user-definable web reports, iAPPS Analytics provides deep insight into areas like visitor usage, content access, age of content, actions taken, and event triggers, and reports on both client and server-side events. iAPPS Analyzer's smart recommendation engine uses this data and identifies actionable solutions enabling our customers to optimize site content and reach their digital campaign goals. There are over 20 standard web reports that come with iAPPS Analyzer. iAPPS Analyzer is uniquely integrated and unified with iAPPS Content Manager, iAPPS Commerce, and iAPPS Marketier; providing our customers with precise information, accurate results, expansion options, and stronger user adoption.

iAPPSds is a web content management and eCommerce platform built specifically to support the needs of multi-unit organizations and franchises. iAPPSds deeply integrates content management, eCommerce, eMarketing, and web analytics and is a self-service web platform that is offered to each authorized franchise or multi-unit organization for a monthly subscription fee. iAPPSds acts as a control center for a large organization's distributed websites enabling local content publishing that is managed through a workflow approval process that gives corporate marketing control of the brand and message. iAPPSds also supports responsive design that adapts to specific device screen sizes access a website, driving more positive user experiences and engagement. iAPPSds is a cloud based SaaS solution.

iAPPS Social is a social media management solution that empowers customers to easily set up customized watch lists tailored by social network, topic, or author to monitor relevant conversations happening on social media, popular websites and blogs. Customers can also prioritize and engage in conversations across the web without ever exiting the iAPPS dashboard and leverage the power of publishing content to department, dealer, franchise or other social media accounts.

Services

Revenue from Digital Engagement Services

Revenue from all digital engagement services is reported as *digital engagement services* in the accompanying consolidated financial statements.

Digital Engagement Services

Digital engagement services address specific customer needs such as digital strategy, web design and web development, usability engineering, information architecture, and Search Engine Optimization (SEO) for their mission critical web site, intranet or online store. Application development engagements are often sold as part of a multiple element arrangement that includes our software products, hosting arrangements (i.e. Managed Service Hosting) that provide for the use of certain hardware and infrastructure at one of our co-managed network operating centers, or retained professional services subsequent to completion of the application development.

Digital Strategy Services

Bridgeline helps customers maximize the effectiveness of their online marketing activities to ensure that their web applications can be exposed to the potential customers that use search engines to locate products and services. Bridgeline's SEO services include competitive analysis, website review, keyword generation, proprietary leading page technology, ongoing registration, monthly reports, and monitoring. Bridgeline's web analytics experts offer consulting and assistance in implementing iAPPS Analyzer or any other type of web analytics package.

Usability Design

By integrating usability into traditional development life cycles, we believe our usability experts can significantly enhance a user's experience. Our usability professionals provide the following services: usability audits, information architecture, process analysis and optimization, interface design and user testing. Our systematic and user-centered approach to application development focuses on developing applications that are intuitive, accessible, engaging, and effective. Our goal is to produce a net effect of increased traffic, improved visitor retention, increased user productivity, reduced user error, lower support cost, and reduced long-term development cost.

Information Architecture

Information Architecture is a design methodology focused on structuring information to ensure that users can find the appropriate data and can complete their desired transactions within a website or application. Understanding users and the context in which users will be initiating with a web application is central to information architecture. Information architects try to put themselves in the position of a typical user of an application to better understand a user's characteristics, behaviors, intentions and motivations. At the same time, the information architect develops an understanding of a web application's functionality and data structures. The understanding of these components enables the architect to make customer centric decisions about the end user and then translate those decisions into site maps, wire frames and clickable prototypes.

Information architecture forms the foundation of a web application's usability. The extent to which a web application is user-friendly and is widely adopted by a user base is primarily dependent on the success of the information architecture. Information architecture defines how well users can navigate through a website or application and how easily they can find the desired information or function. As digital engagement becomes more standard and commoditized, information architecture will increase as a differentiator for application developers.

Managed Service Hosting

Revenue from Managed Service Hosting

Revenue from managed service hosting is reported as *managed service hosting* in the accompanying consolidated financial statements.

A large number of our customers engage Bridgeline to host and manage the mission critical web sites and web stores we develop. Through our partnerships with Internap, a Tier 1 secured data center, we offer co-location services in state-of-the-art facilities. We provide 24/7 application monitoring, emergency response, version control, load balancing, managed firewall security, and virus protection services. We provide shared hosting, dedicated hosting, and SaaS hosting for our customers.

Sales and Marketing

Overview

Bridgeline employs a direct sales force to sell enterprise iAPPS engagements and each sale takes on average 180 days to complete. Our direct sales force focuses its efforts selling to mid-sized and large companies. These companies are generally categorized in the following vertical markets: financial services, retail brand names, health services and life sciences, technology (software and hardware), and associations and foundations.

Bridgeline also employs a direct sales force to sell iAPPSds engagements to franchises and multi-unit organizations. Each sale in this vertical market takes on average approximately one year to complete.

We have ten geographic locations in the United States with full-time professional direct sales personnel. Our geographic locations are in the metropolitan Atlanta, Baltimore, Boston, Chicago, Dallas, Denver, New York, San Diego, San Luis Obispo, and Tampa areas.

Strategic Alliances

We have dedicated business development professionals whose mission is to identify and establish strategic alliances for iAPPS and iAPPSds. In June 2012, Bridgeline announced a strategic alliance with UPS Logistics. Bridgeline and UPS Logistics signed a multi-year agreement to offer B2B and B2C eCommerce web stores with an end-to-end eCommerce offering comprised of Bridgeline's eCommerce Fulfilled™ solution and UPS Logistics and fulfillment services. The combined Bridgeline and UPS Logistics offering provides customers with the ability to manage the eCommerce and supply chain fulfillment needs and was designed to benefit mid-market and larger online web stores who seek end to end solutions.

In July of 2012 Bridgeline signed a multi-year agreement with The UPS Stores, a national franchise network of over 4,300 locations who license the iAPPSds platform.

We continue to pursue other significant strategic alliances that will enhance the sales and distribution opportunities of iAPPS related intellectual property.

Engagement Methodology

We use an accountable, strategic engagement process developed specifically for target companies that require a technology based professional approach. We believe it is critical to qualify each opportunity and to assure our skill set and tools match up well with customer's needs. As an essential part of every engagement, we believe our engagement methodology streamlines our customer qualification process, strengthens our customer relationships, ensures our skill set and tools match the customer's needs, and results in the submission of targeted proposals.

Organic Growth from Existing Customer Base

We have specific proactive programs that consistently market our iAPPS platform and interactive development capabilities. Our business development professionals seek ongoing business opportunities within our existing customer base and within other operating divisions or subsidiaries of our existing customer base.

New Customer Acquisition

We identify customers within our vertical expertise (financial services, franchise/dealer networks, retail brand names, health services and life sciences, high technology, and associations and foundations). Our business development professionals create an annual territory plan identifying various strategies to engage our target customers. These territory plans are evaluated and updated every 60 days.

Customer Retention Programs

We use digital marketing capabilities when marketing to our customer base. We make available via email and on our website Bridgeline authored Whitepapers, featured case studies, and/or Company related announcements to our customers on a bimonthly basis. We also host educational on-line webinars, face to face seminars and training.

New Lead Generation Programs

We generate targeted leads and new business opportunities by leveraging on-line marketing strategies. We receive leads by maximizing the SEO capabilities of our own website. Through our website, we provide various educational Whitepapers and promote upcoming on-line seminars. In addition, we utlilize banner advertisements on various independent newsletters and paid search advertisements that are linked to our website. We also participate and exhibit at targeted events.

Social Media Programs

We market Bridgeline's upcoming events, Whitepapers, blogs, case studies, digital product tutorials, announcements, and related articles frequently on leading social media platforms such as Twitter, LinkedIn, YouTube and Facebook.

Acquisitions

Bridgeline will continue to evaluate expanding its distribution of iAPPS and its interactive development capabilities through acquisitions.

There were no acquisitions during the fiscal year ended September 30, 2014 and one acquisition during the fiscal year ended September 30, 2013 as described below.

ElementsLocal

On August 1, 2013, we completed the acquisition of ElementsLocal, a California based developer of a SaaS website platform for the franchise marketplace. ElementsLocal has over 3,200 franchises on its web platform. We acquired all of the outstanding capital stock of ElementsLocal for consideration consisting of (i) $463 thousand in cash, (ii) $604 thousand in shares of Bridgeline Digital common stock (valued at $1.15 per share), (iii) assumption of $188 thousand of indebtedness and (iv) contingent consideration of up to $904 thousand in cash and $396 thousand in shares of Bridgeline Digital common stock. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving a certain quarterly revenue target during the period. The contingent common stock payable each earnout period is determined by dividing $33 thousand by the greater of: (i) the average closing price for Bridgline Digitial common stock for the 30 day trading period preceding the end of the earnout period, or (ii) $1.17. To the extent that a quarterly revenue target is not met in a particular quarter, the earn-out period will be extended for up to four additional quarters. ElementsLocals operating results are reflected in the condensed consolidated financial statements as of the acquisition date.

Research and Development

We have a strong commitment to research and development activities focusing on creating new products and innovations, product enhancements, and funding future market opportunities. In fiscal 2014 and 2013, research and development expenses were $2.4 million, or 10% of revenues, and $1.4 million, or 6% of revenues, respectively.

Employees

We have 135 employees worldwide as of September 30, 2014. Substantially all of those employees are full time employees.

Customers

We primarily serve the following vertical markets that we believe have a history of investing in information technology enhancements and initiatives as follows:

Financial Services
Franchises/Multi-unit Organizations
Retail Brand Names
Health Services and Life Sciences
Technology (software and hardware)
Associations and Foundations

For the years ended September 30, 2014 and 2013, no customer generated more than 10% of our revenue. We will focus our efforts to engage with customers that are aligned with the Company's core competencies and will continue to proactively end engagements with a number of smaller hosting customers obtained through previous acquisitions.

Competition

The markets for our products and services, including software for web content management, eCommerce platform software, eMarketing software, web analytics software and digital engagement services are highly competitive, fragmented, and rapidly changing. Barriers to entry in such markets remain relatively low. The markets are significantly affected by new product introductions and other market activities of industry participants. With the introduction of new technologies and market entrants, we expect competition to persist and intensify in the future.

We believe we compete adequately with others and we distinguish ourselves from our competitors in a number of ways:

We believe our competitors generally offer their web application software typically as a single point of entry type product (such as content management only, or commerce only) as compared to the deeply integrated approach as provided by the iAPPS platform.

We believe our competitors can generally only deploy their solutions in either a Cloud/SaaS environment or in a dedicated server environment. The iAPPS platform's architecture is flexible and is capable of being deployed in either a Cloud/SaaS or dedicated server environment.

We believe the majority of our competitors do not provide interactive technology development services that complement their software products. Our ability to develop mission critical web sites and online stores on our own deeply integrated iAPPS platform providing a quality end-to-end solution that distinguishes us from our competitors.

We believe the interface of the iAPPS platform has been designed for ease of use without substantial technical skills.

Finally, we believe the iAPPS platform offers a competitive price-to-functionality ratio when compared to our competitors.

Available Information

This Annual Report on Form 10-K, as well as our quarterly reports on Form 10-Q and current reports on Form 8-K, along with any amendments to those reports, are made available upon request, on our website www.bridgeline.com as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission. Copies of the following are also available through our website on the "About Us - Investor Information" page under the caption "Governance" and are available in print to any shareholder who requests it:

Code of Business Ethics
Committee Charters for the following Board Committees:
o Nominating and Corporate Governance Committee

o Audit Committee

o Compensation Committee

The public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. Information regarding the SEC's Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site that contains reports, proxy and information statements, and other information and can be found at http://www.sec.gov.

Item 1A. Risk Factors

This report contains forward-looking statements that involve risks and uncertainties, such as statements of our objectives, expectations and intentions. The cautionary statements made in this report are applicable to all forward-looking statements wherever they appear in this report. Our actual results could differ materially from those discussed herein. In addition to the risks discussed in "Management's Discussion and Analysis of Financial Condition and Results of Operations," our business is subject to the risks set forth below.

We operate in a rapidly changing environment that involves certain risks and uncertainties, some of which are beyond our control. The risks described below are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also materially adversely affect our business, financial condition and/or operating results.

If we are unable to manage our future growth efficiently, our business, liquidity, revenues and profitability may suffer.

We anticipate that continued expansion of our core business will require us to address potential market opportunities. For example, we may need to expand the size of our research and development, sales, corporate finance or operations staff. There can be no assurance that our infrastructure will be sufficiently flexible and adaptable to manage our projected growth or that we will have sufficient resources, human or otherwise, to sustain such growth. If we are unable to adequately address these additional demands on our resources, our profitability and growth might suffer. Also, if we continue to expand our operations, management might not be effective in expanding our physical facilities and our systems, procedures or controls might not be adequate to support such expansion. Our inability to manage our growth could harm our business and decrease our revenues.

We may also require additional funding to further expand our business. We currently have a borrowing facility with Bridge Bank from which we can borrow, and this line is subject to financial covenants that must be met. It is not certain that all or part of this line will be available to us in the future; and other sources of financing may not be available to us in a timely basis if at all, or on terms acceptable to us. If we fail to obtain acceptable funding when needed, we may not have sufficient resources to fund our normal operations, and this would have a material adverse effect on our business.

Our revenue and quarterly results may fluctuate, which could adversely affect our stock price.

We have experienced, and may in the future experience, significant fluctuations in our quarterly operating results that may be caused by many factors. These factors include:

- changes in demand for our products;
- introduction, enhancement or announcement of products by us or our competitors;
- market acceptance of our new products;
- the growth rates of certain market segments in which we compete;
- size and timing of significant orders;
- budgeting cycles of customers;
- mix of products and services sold;
- changes in the level of operating expenses;
- completion or announcement of acquisitions; and
- general economic conditions in regions in which we conduct business.

The length of our sales cycle can fluctuate significantly which could result in significant fluctuations in license revenues being recognized from quarter to quarter.

The decision by a customer to purchase our products often involves the development of a complex implementation plan across a customer’s business. This process often requires a significant commitment of resources both by prospective customers and us. Given the significant investment and commitment of resources required in order to implement our software, it may take several months, or even several quarters, for marketing opportunities to materialize. If a customer's decision to purchase our products is delayed or if the installation of our products takes longer than originally anticipated, the date on which we may recognize revenues from these sales would be delayed. Such delays and fluctuations could cause our revenues to be lower than expected in a particular period and we may not be able to adjust our costs quickly enough to offset such lower revenue, potentially negatively impacting our results of operations.

Because most of our licenses are renewable on an annual basis, a reduction in our license renewal rate could reduce our revenue.

Our customers have no obligation to renew their annual subscription licenses, and some customers have elected not to do so. Our license renewal rates may decline or fluctuate as a result of a number of factors, including customer dissatisfaction with our products and services, our failure to update our products to maintain their attractiveness in the market, or constraints or changes in budget priorities faced by our customers. A decline in license renewal rates could cause our revenue to decline which would have a material adverse effect on our operations.

We face intense and growing competition, which could result in price reductions, reduced operating margins and loss of market share.

We operate in a highly competitive marketplace and generally encounter intense competition to create and maintain demand for our services and to obtain service contracts. If we are unable to successfully compete for new business and license renewals, our revenue growth and operating margins may decline. The market for our iAPPS platform (Content Manager, Analyzer, eCommerce, Marketier, Social) and web development services are competitive and rapidly changing. Barriers to entry in such markets are relatively low. With the introduction of new technologies and market entrants, we expect competition to intensify in the future. Some of our principal competitors offer their products at a lower price, which may result in pricing pressures. Such pricing pressures and increased competition generally could result in reduced sales, reduced margins or the failure of our product and service offerings to achieve or maintain more widespread market acceptance.

The web development/services market is highly fragmented with a large number of competitors and potential competitors. Our prominent public company competitors are Open Text, Demandware, Digital River, GSI Commerce, and Adobe. We face competition from customers and potential customers who develop their own applications internally. We also face competition from potential competitors that are substantially larger than we are and who have significantly greater financial, technical and marketing resources, and established direct and indirect channels of distribution. As a result, they are able to devote greater resources to the development, promotion and sale of their products than we can.

There may be a limited market for our common stock which may make it more difficult for you to sell your stock and which may reduce the market price of our common stock.

The average shares traded per day in fiscal 2014 was approximately 95,000 shares per day compared to approximately 50,000 for fiscal 2013. If our average trading volume of our common stock were to decrease it may impair the ability of holders of our common stock to sell their shares at the time they wish to sell them or at a price that they consider reasonable. The low trading volume may also reduce the fair market value of the shares of our common stock. Accordingly, there can be no assurance that the price of our common stock will reflect our actual value. There can be no assurance that the daily trading volume of our common stock will increase or improve either now or in the future.

The market price of our common stock is volatile which could adversely affect your investment in our common stock.

The market price of our common stock is volatile and could fluctuate significantly for many reasons, including, without limitation: as a result of the risk factors listed in this annual report on Form 10-K; actual or anticipated fluctuations in our operating results; and general economic and industry conditions. During fiscal 2014, the closing price of our common stock as reported by NASDAQ fluctuated between $0.65 and $1.36.

We will not be able to maintain our listing on the NASDAQ Capital Market if we are unable to satisfy NASDAQ's minimum bid price requirements of $1.00 per share.

We are currently not in compliance with the requirements for listing on the NASDAQ Capital Market. We are required to meet certain financial criteria in order to maintain our listing on the NASDAQ Capital Market. One such requirement is that we maintain a minimum closing bid price of at least $1.00 per share for our common stock. Because our stock traded below $1.00 per share for 30 consecutive business days, on May 28, 2014, The Nasdaq Stock Market ("Nasdaq") notified us that we were not in compliance with Marketplace Rule 5550(a)(2). We were provided 180 calendar days, or until November 24, 2014, to regain compliance with the minimum closing bid price requirement. On December 1, 2014, we were notified by Nasdaq that we are eligible for an additional 180 calendar day period, or until May 26, 2015 to regain compliance. If at any time during this additional time period the closing bid price of our stock price is at least $1.00 per share for a minimum of 10 consecutive business days, then we can regain compliance.

If we are unable to demonstrate compliance by May 26, 2015 then our shares of common stock will be subject to delisting. At that point, the Nasdaq staff will determine whether we meet the NASDAQ Capital Market initial listing criteria, except for the minimum bid price requirement. If NASDAQ determines that we meet the initial listing criteria, the NASDAQ staff will grant us an additional 180 calendar day compliance period. If we are not eligible for an additional compliance period, the NASDAQ staff will provide written notice that our securities will be delisted from the NASDAQ Capital Market.

The delisting of our common stock could have a negative effect on the market price for our shares.

If our common stock is delisted from NASDAQ it may be traded on the OTCQX or the OTC Bulletin Board which may limit the market for our stock and affect our ability to raise capital.

We are currently not in compliance with the requirements for listing on the NASDAQ Capital Market. If our common stock is delisted from NASDAQ, we will apply to have our common stock quoted on the OTCQX, the world's largest interdealer quotation system, which is operated by OTC Market Groups, Inc. Our stock may also be traded on the OTC Bulletin Board.

There may be a limited market for our common stock if it is quoted on the OTCQX or the OTC Bulletin Board. Trading in our stock may become more difficult and our share price could decrease. Specifically, you may not be able to resell your shares of common stock at or above the price you paid.

In addition, the delisting of our common stock from NASDAQ may impair our ability to raise additional capital due to the less liquid nature of the OTCQX and OTC Bulletin Board markets. While we cannot guarantee that we would be able to complete an equity financing on acceptable terms, or at all, we believe that dilution from any equity financing while our shares are quoted on an over-the-counter market would likely be substantially greater than if we were to complete a financing while our common stock is traded on a national securities exchange. Further, if our common stock is not traded on an exchange, we will no longer be eligible to use short-form registration statements on Form S-3 for the registration of our securities, which could impair our ability to raise additional capital as needed.

If our products fail to perform properly due to undetected errors or similar problems, our business could suffer, and we could face product liability exposure.

We develop and sell complex web engagement software which may contain undetected errors, or bugs. Such errors can be detected at any point in a product's life cycle, but are frequently found after introduction of new software or enhancements to existing software. We continually introduce new products and new versions of our products. Despite internal testing and testing by current and potential customers, our current and future products may contain serious defects. If we detect any errors before we ship a product, we might have to delay product shipment for an extended period of time while we address the problem. We might not discover software errors that affect our new or current products or enhancements until after they are deployed, and we may need to provide enhancements to correct such errors. Therefore, it is possible that, despite our testing, errors may occur in our software. These errors could result in the following:

- harm to our reputation;
- lost sales;
- delays in commercial release;
- product liability claims;
- contractual disputes;
- negative publicity;
- delays in or loss of market acceptance of our products;
- license terminations or renegotiations; or
- unexpected expenses and diversion of resources to remedy errors.

Furthermore, our customers may use our software together with products from other companies. As a result, when problems occur, it might be difficult to identify the source of the problem. Even when our software does not cause these problems, the existence of these errors might cause us to incur significant costs, divert the attention of our technical personnel from our product development efforts, impact our reputation, or cause significant customer relations problems.

Technology and customer requirements evolve rapidly in our industry, and if we do not continue to develop new products and enhance our existing products in response to these changes, our business could suffer.

We will need to continue to enhance our products in order to maintain our competitive position. We may not be successful in developing and marketing enhancements to our products on a timely basis, and any enhancements we develop may not adequately address the changing needs of the marketplace. Overlaying the risks associated with our existing products and enhancements are ongoing technological developments and rapid changes in customer requirements. Our future success will depend upon our ability to develop and introduce in a timely manner new products that take advantage of technological advances and respond to new customer requirements. The development of new products is increasingly complex and uncertain, which increases the risk of delays. We may not be successful in developing new products and incorporating new technology on a timely basis, and any new products may not adequately address the changing needs of the marketplace. Failure to develop new products and product enhancements that meet market needs in a timely manner could have a material adverse effect on our business, financial condition and operating results.

If we are unable to protect our proprietary technology and other intellectual property rights, our ability to compete in the marketplace may be substantially reduced.

If we are unable to protect our intellectual property, our competitors could use our intellectual property to market products similar to our products, which could decrease demand for such products, thus decreasing our revenue. We rely on a combination of copyright, trademark and trade secret laws, as well as licensing agreements, third-party non-disclosure agreements and other contractual measures, to protect our intellectual property rights. These protections may not be adequate to prevent our competitors from copying or reverse-engineering our products. Our competitors may independently develop technologies that are substantially similar or superior to our technology. To protect our trade secrets and other proprietary information, we require employees, consultants, advisors and collaborators to enter into confidentiality agreements. These agreements may not provide meaningful protection for our trade secrets, know-how or other proprietary information in the event of any unauthorized use, misappropriation or disclosure of such trade secrets, know-how or other proprietary information. The protective mechanisms we include in our products may not be sufficient to prevent unauthorized copying. Existing copyright laws afford only limited protection for our intellectual property rights and may not protect such rights in the event competitors independently develop similar products. In addition, the laws of some countries in which our products are or may be licensed do not protect our products and intellectual property rights to the same extent as do the laws of the United States.

Policing unauthorized use of our products is difficult, and litigation could become necessary in the future to enforce our intellectual property rights. Any litigation could be time consuming and expensive to prosecute or resolve, result in substantial diversion of management attention and resources, and materially harm our business or financial condition.

If a third party asserts that we infringe upon its proprietary rights, we could be required to redesign our products, pay significant royalties or enter into license agreements.

Claims of infringement are becoming increasingly common as the software industry develops and as related legal protections, including but not limited to patents, are applied to software products. Although we do not believe that our products infringe on the rights of third parties, a third party may assert that our technology or technologies of entities we acquire violates its intellectual property rights. As the number of software products in our markets increases and the functionality of these products further overlap, we believe that infringement claims will become more common. Any claims against us, regardless of their merit, could:

- be expensive and time consuming to defend;
- result in negative publicity;
- force us to stop licensing our products that incorporate the challenged intellectual property;
- require us to redesign our products;
- divert management’s attention and our other resources; and or

require us to enter into royalty or licensing agreements in order to obtain the right to use necessary technologies, which may not be available on terms acceptable to us, if at all.

We believe that any successful challenge to our use of a trademark or domain name could substantially diminish our ability to conduct business in a particular market or jurisdiction and thus decrease our revenue and result in possible losses to our business.

If the security of our software, in particular the hosted Internet solutions products we have developed, is breached, our business and reputation could suffer.

Fundamental to the use of our products is the secure collection, storage and transmission of confidential information. Third parties may attempt to breach our security or that of our customers and their databases. We might be liable to our customers for any breach in such security, and any breach could harm our customers, our business and reputation. Any imposition of liability, particularly liability that is not covered by insurance or is in excess of insurance coverage, could harm our reputation, business and operating results. Computers, including those that utilize our software, are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We might be required to expend significant capital and other resources to protect further against security breaches or to rectify problems caused by any security breach, which, in turn could divert funds available for corporate growth and expansion or future acquisitions.

If our co-managed network operations center that houses our iAPPS SaaS environment and managed service hosting were to experience a disruption in service, our business and reputation could suffer.

We host our SaaS and managed hosting customers from our co-managed network operation center (“NOC”), which is operated by a third-party. While we have ownership control and have access to our servers and all of the components of our network operation center, we do not control the operation of the Tier-1 data facility. Our data facility lease expires in 2014 with an automatic renewal of one year. If upon renewal date our third-party provider does not provide commercially reasonable terms, we may be required to transfer our servers to a new data center facility, and we may incur significant costs and possible service interruption in connection with doing so.

Problems faced by our third-party data center location, with the telecommunications network providers with whom we or they contract, or with the systems by which our telecommunications providers allocate capacity among their customers, including us, could adversely affect the experience of our customers. Our third-party data center operator could decide to close their facilities without adequate notice. In addition, any financial difficulties, such as bankruptcy, faced by our third-party data center operators or any of the service providers with whom we or they contract may have negative effects on our business, the nature and extent of which are difficult to predict. Additionally, if our data center is unable to keep up with our growing needs for capacity, this could have an adverse effect on our business. Any changes in third-party service levels at our data centers or any errors, defects, disruptions, or other performance problems with our services could harm our reputation. Interruptions in our services might reduce our revenue, cause us to issue credits or refunds to customers, subject us to potential liability, or harm our renewal rates.

We are dependent upon our management team, and the loss of any of these individuals could harm our business.

We are dependent on the efforts of our key management personnel. The loss of any of our key management personnel, or our inability to recruit and train additional key management and other personnel in a timely manner, could materially and adversely affect our business, operations and future prospects. We do not maintain a key man insurance policy covering any of our employees. In addition, in the event that Thomas Massie, our founder, Chairman and Chief Executive Officer, is terminated by us without cause, he is entitled to receive severance payments equal to three years' total compensation, including bonus amounts. In the event we are required to pay the severance payments to Mr. Massie, it could have a material adverse effect on our results of operations for the fiscal quarter and year in which such payments are made.

Because competition for highly qualified personnel is intense, we might not be able to attract and retain the employees we need to support our planned growth.

We will need to increase the size and maintain the quality of our sales force, software development staff and professional services organization to execute our growth plans. To meet our objectives, we must attract and retain highly qualified personnel with specialized skill sets. Competition for qualified personnel can be intense, and we might not be successful in attracting and retaining them. Our ability to maintain and expand our sales, product development and professional services teams will depend on our ability to recruit, train and retain top quality people with advanced skills who understand sales to, and the specific needs of, our target customers. For these reasons, we have experienced, and we expect to again experience in the future, challenges in hiring and retaining highly skilled employees with appropriate qualifications for our business. In addition to hiring services personnel to meet our needs, we may also engage additional third-party consultants as contractors, which could have a negative impact on our financial results. If we are unable to hire or retain qualified personnel, or if newly hired personnel fail to develop the necessary skills or reach productivity slower than anticipated, it would be more difficult for us to sell our products and services, and we could experience a shortfall in revenue and not achieve our planned growth.

Future acquisitions may be difficult to integrate into our existing operations, may disrupt our business, dilute stockholder value, divert management’s attention, or negatively affect our operating results.

We have acquired multiple businesses since our inception in 2000. A key element of our growth and market share expansion strategy has been the pursuit of additional acquisitions in the fragmented digital engagement industry in the future. These future acquisitions may create risks such as: (i) the need to integrate and manage the businesses and products acquired with our own business and products; (ii) additional demands on our resources, systems, procedures and controls; (iii) disruption of our ongoing business; (iv) unknown liabilities associated with the acquired businesses; and (v) diversion of management's attention from other business concerns. In addition, future acquisitions could involve substantial investment of funds or financings by issuance of debt or equity securities and could result in one-time charges and expenses and have the potential to either dilute the interests of existing shareholders or result in the issuance of or assumption of debt. Any such acquisition may not be successful in generating revenues, income or other returns to us, and the resources committed to such activities will not be available to us for other purposes. Moreover, if we are unable to access capital markets on acceptable terms or at all, we may not be able to consummate acquisitions, or may have to do so based upon less than optimal capital structure. Our inability to take advantage of growth opportunities for our business or to address risks associated with acquisitions or investments in businesses may negatively affect our operating results. Additionally, any impairment of goodwill or other intangible assets acquired in an acquisition or in an investment, or charges to earnings associated with any acquisition or investment activity, may materially reduce our earnings which, in turn, may have an adverse material effect on the price of our common stock.

Increasing government regulation could affect our business and may adversely affect our financial condition.

We are subject not only to regulations applicable to businesses generally, but also to laws and regulations directly applicable to electronic commerce. Although there are currently few such laws and regulations, state, federal and foreign governments may adopt laws and regulations applicable to our business. Any such legislation or regulation could dampen the growth of the Internet and decrease its acceptance. If such a decline occurs, companies may choose in the future not to use our products and services. Any new laws or regulations in the following areas could affect our business:

- user privacy;
- the pricing and taxation of goods and services offered over the Internet;
- the content of websites;
- copyrights;
- consumer protection, including the potential application of "do not call" registry requirements on customers and consumer backlash in general to direct marketing efforts of customers;
- the online distribution of specific material or content over the Internet; or
- the characteristics and quality of products and services offered over the Internet.

We have never paid dividends and we do not anticipate paying dividends in the future.

We have never paid cash dividends and do not believe that we will pay any cash dividends on our common stock in the future. Since we have no plan to pay cash dividends, an investor would only realize income from his investment in our shares if there is a rise in the market price of our common stock, which is uncertain and unpredictable.

Item 1B. Unresolved Staff Comments

Not required.

Item 2. Properties.

The following table lists our offices, all of which are leased:

Geographic Location	**Address**	**Size**
Atlanta, Georgia	5555 Triangle Parkway Norcross, Georgia 30092	8,547 square feet, professional office space
Baltimore, Maryland	6711 Columbia Gateway Dr. Baltimore, Maryland 21046	4,925 square feet, Professional office space
Bangalore, India	Inner Ring Road Bangalore 560 052	14,302 square feet professional office space
Boston, Massachusetts	80 Blanchard Road Burlington, Massachusetts 01803	21,136 square feet, professional office space
Chicago, Illinois	30 N. LaSalle Street, 20th Floor Chicago, IL 60602	4,880 square feet, professional office space
Dallas, Texas	4975 Preston Park Boulevard, Suite 550 Plano, TX 75093	5,641 square feet, professional office space
Denver, Colorado	410 17th Street, Suite 600 Denver, CO 80202	5,993 square feet, professional office space
New York, New York	450 7th Avenue New York, NY 10123	5,582 square feet, professional office space
San Diego, California	6240 Cornerstone Suite 110 San Diego, CA 92121	2,560 square feet Professional office space
San Luis Obispo, California	3450 Broad Street San Luis Obispo, CA 93401	3,937 square feet Professional office space
Tampa, Florida	5325 Primrose Lake Circle Tampa, FL 33647	4,264 square feet Professional office space

Item 3. Legal Proceedings.

From time to time we are subject to ordinary routine litigation and claims incidental to our business. We are not currently involved in any legal proceedings that we believe are material beyond those described below.

Bridgeline Digital, Inc vs. e.Magination Network, LLC and its principal owner, Daniel Roche.

In August 2010, Bridgeline initiated a lawsuit against e.Magination network, LLC and its principal owner, Daniel Roche, in the Federal District Court of Massachusetts. On August 6, 2013 the parties entered into a settlement agreement pursuant to which Bridgeline agreed to pay Mr. Roche a total of $468 thousand, as well as the payment of previously earned contingent consideration which was accrued at the date of acquisition. This claim was settled in full during fiscal 2014.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

Item 5. Market for Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities.

The following table sets forth, for the periods indicated, the range of high and low sale prices for our common stock. Our common stock trades on the NASDAQ Capital Market under the symbol BLIN.

Year Ended September 30, 2014	**High**	**Low**
Fourth Quarter	$0.93	$0.65
Third Quarter	$1.02	$0.76
Second Quarter	$1.36	$0.88
First Quarter	$1.16	$0.79
Year Ended September 30, 2013	**High**	**Low**
Fourth Quarter	$1.33	$1.00
Third Quarter	$1.30	$0.99
Second Quarter	$1.80	$1.25
First Quarter	$2.40	$1.20

We have not declared or paid cash dividends on our common stock and do not plan to pay cash dividends to our shareholders in the near future. As of December 5, 2014, our common stock was held of record by approximately 1,486 shareholders. Most of the Company’s stock is held in street name through one or more nominees.

Recent Sales of Unregistered Securities; Use of Proceeds From Registered Securities

The following summarizes all sales of our unregistered securities during the year ended September 30, 2014, other than sales of unregistered securities during the quarter ended March 31, 2014 that were previously disclosed on Form 8-K. The securities in the below-referenced transactions were (i) issued without registration and (ii) were subject to restrictions under the Securities Act and the securities laws of certain states, in reliance on the private offering exemptions contained in Sections 4(2), 4(6) and/or 3(b) of the Securities Act and on Regulation D promulgated there under, and in reliance on similar exemptions under applicable state laws as transactions not involving a public offering. Unless stated otherwise, no placement or underwriting fees were paid in connection with these transactions.

During the year ended September 30, 2014, the Company granted 1,197,500 stock options under its Amended and Restated Stock Incentive Plan at a weighted average exercise price of $1.10 per share.

The securities were issued exclusively to our directors, executive officers and employees. The issuance of options and the shares of common stock issuable upon the exercise of such options as described above were issued pursuant to written compensatory plans or arrangements with our employees, directors and consultants, in reliance on the exemptions from the registration provisions of the Securities Act set forth in Section 4(2) thereof relative to sales by an issuer not involving any public offering, to the extent an exemption from such registration was required.

Item 6. Selected Financial Data.

Not required.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

This section contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of a variety of factors and risks including the impact of the weakness in the U.S. and international economies on our business, our inability to manage our future growth effectively or profitably, fluctuations in our revenue and quarterly results, our license renewal rate, the impact of competition and our ability to maintain margins or market share, the limited market for our common stock, the volatility of the market price of our common stock, the ability to maintain our listing on the NASDAQ Capital Market, the ability to raise capital, the performance of our products, our ability to respond to rapidly evolving technology and customer requirements, our ability to protect our proprietary technology, the security of our software, our dependence on our management team and key personnel, our ability to hire and retain future key personnel, or our ability to maintain an effective system of internal controls. These and other risks are more fully described herein and in our other filings with the Securities and Exchange Commission.

This section should be read in combination with the accompanying audited consolidated financial statements and related notes prepared in accordance with United States generally accepted accounting principles.

Overview

Bridgeline Digital, The Digital Engagement Company™, enables its customers to maximize the performance of their mission critical websites, intranets, and online stores. Bridgeline's iAPPS® platform deeply integrates Web Content Management, eCommerce, eMarketing, Social Media management, and Web Analytics to help marketers deliver online experiences that attract, engage and convert their customers across all digital channels. Bridgeline's iAPPS platform combined with its digital services assists customers in maximizing on-line revenue, improving customer service and loyalty, enhancing employee knowledge, and reducing operational costs.

In fiscal 2012, Bridgeline Digital announced the release of iAPPSds ("distributed subscription"), a platform that empowers franchise and multi-unit organizations with state-of-the-art web engagement management while providing superior oversight of corporate branding. iAPPSds deeply integrates content management, eCommerce, eMarketing and web analytics and is a self-service web platform that is offered to each authorized franchise or dealer for a monthly subscription fee. On August 1, 2013, we acquired franchise web developer ElementsLocal, expanding Bridgeline Digital's presence in the franchise market place.

The iAPPS platform is delivered through a cloud-based SaaS ("Software as a Service") multi-tenant business model, whose flexible architecture provides customers with state of the art deployment providing maintenance, daily technical operation and support; or via a traditional perpetual licensing business model, in which the iAPPS software resides on a dedicated server in either the customer's facility or Bridgeline's co-managed hosting facility.

iAPPS Content Manager and iAPPS Commerce were selected as finalists for the 2014, 2013, and 2012 CODiE Awards for Best Content Management Solution and Best Electronic Commerce Solution, globally. In 2014, Bridgeline Digital won ten Horizon Interactive Awards for outstanding development of web applications and websites and won fifteen Horizon Interactive Awards in 2013. Also in 2013, the Web Marketing Association sponsored Internet Advertising Competition honored Bridgeline Digital with three awards for iAPPS customer websites and B2B Magazine selected Bridgeline Digital as one of the Top Interactive Technology companies in the United States. In 2013, KMWorld Magazine Editors selected Bridgeline Digital as one of the 100 Companies That Matter in Knowledge Management and also selected iAPPS as a Trend Setting Product in 2013.

Bridgeline Digital was incorporated under the laws of the State of Delaware on August 28, 2000.

Locations

The Company's corporate office is located in Burlington, Massachusetts. The Company maintains regional field offices serving the following geographical locations: Atlanta, Baltimore, Boston, Chicago, Dallas, Denver, New York, San Diego, San Luis Obispo and Tampa. The Company has one wholly-owned subsidiary, Bridgeline Digital Pvt. Ltd. located in Bangalore, India.

Sales and Marketing

Bridgeline employs a direct sales force and each sale takes on average 180 days to complete. Each franchise/multi-unit organization sale takes on average 365 days to complete. Our direct sales force focuses its efforts selling to medium-sized and large companies. These companies are generally categorized in the following vertical markets: (i) financial services; (ii) franchises/multi-unit organizations; (iii) retail brand names; (iv) health services and life sciences; (v) technology (software and hardware); and (vi) associations and foundations. We have ten geographic locations in the United States with full-time professional direct sales personnel.

We have business development professionals dedicated to identifying and establishing strategic alliances for iAPPS and iAPPSds. In 2012, Bridgeline announced a strategic alliance with UPS Logistics. Bridgeline and UPS Logistics signed a multi-year agreement to offer B2B and B2C eCommerce web stores with an end-to-end eCommerce offering comprised of Bridgeline's eCommerce Fulfilled™ solution and UPS Logistics and fulfillment services. The combined Bridgeline and UPS Logistics offering provides customers with the ability to manage the eCommerce and supply chain fulfillment needs and was designed to benefit mid-market and larger online web stores who seek end to end solutions. Also, in 2012, we signed a multi-year agreement with The UPS Stores, a national franchise network of over 4,300 locations who license the iAPPS ds platform.

In 2013, we signed a multi-year agreement with a national provider of outsourced sales services with over 300 locations. We also added national brand names such as Sport Clips®, Glass Doctor® and Maaco® to our list of franchise customers via the ElementsLocal acquisition. In 2014, we signed two more national multi-unit organizations expanding the iAPPSds footprint to potentially thousands more customers.

We continue to pursue significant strategic alliances that will enhance the sales and distribution opportunities of iAPPS related intellectual property.

Acquisitions

Bridgeline will continue to evaluate expanding its distribution of iAPPS and its interactive development capabilities through acquisitions.

During the fiscal year ended September 30, 2013, we completed one acquisition. On August 1, 2013, we completed the acquisition of ElementsLocal, a California based developer of an online SaaS platform for the franchise marketplace. ElementsLocal had over 3,200 franchises on its platform.

The operating results of ElementsLocal is reflected in the condensed consolidated financial statements as of the acquisition date.

We may make additional acquisitions in the foreseeable future. These potential acquisitions are consistent with our iAPPS platform distribution strategy and growth strategy by providing Bridgeline with new geographical distribution opportunities, an expanded customer base, an expanded sales force and an expanded developer force. In addition, integrating acquired companies into our existing operations allows us to consolidate the finance, human resources, legal, marketing, research and development of the acquired businesses with our own internal resources, hence reducing the aggregate of these expenses for the combined businesses and resulting in improved operating results.

Customer Information

We currently have approximately 2,500 active customers. For the years ended September 30, 2014 and 2013, no one customer represented 10% or more of the Company's total revenue.

Summary of Results of Operations

Total revenue for the fiscal year ended September 30, 2014 ("fiscal 2014") decreased to $23.7 million from $24.5 million for the fiscal year ended September 30, 2013 ("fiscal 2013"). Loss from operations for fiscal 2014 was ($5.2) million compared with loss from operations of ($3.2) million for fiscal 2013. We had a net loss for fiscal 2014 of ($6.2) million compared with a net loss of ($3.6) million for fiscal 2013. Loss per share for fiscal 2014 was ($0.32) compared with loss per share of ($0.23) for fiscal 2013.

Summary of Fiscal 2014

Financial

Total subscription and perpetual license revenue increased 44% to $5.7 million in fiscal 2014 from $4.0 million in fiscal 2013.

Recurring revenue, which reflects amounts that are contractually due to Bridgeline, increased 33% to $6.9 million in fiscal 2014 from $5.2 million in fiscal 2013.

Total iAPPS related revenue increased 8% to $20.3 million in fiscal 2014 from $18.8 million in fiscal 2013.

Non-iAPPS related revenue decreased 40% in fiscal 2014 compared to fiscal 2013.

RESULTS OF OPERATIONS

(dollars in thousands)	Year Ended September 30, 2014	2013	$ Change	% Change
Revenue				
Digital engagement services				
iAPPS digital engagement services	$14,308	$14,733	$(425)	(3%)
% of total revenue	60%	60%		
Other digital engagement services	2,061	3,852	(1,791)	(46%)
% of total revenue	9%	16%		
Subtotal digital engagement services	16,369	18,585	(2,216)	(12%)
% of total revenue	69%	76%		
Subscription and perpetual licenses	5,749	4,000	1,749	44%
% of total revenue	24%	16%		
Managed service hosting	1,619	1,921	(302)	(16%)
% of total revenue	7%	8%		
Total revenue	**23,737**	**24,506**	**(769)**	**(3%)**
Cost of revenue				
Digital engagement services				
iAPPS digital engagement cost	9,071	7,808	1,263	16%
% of iAPPS digital engagement revenue	63%	53%		
Other digital engagement cost	1,160	2,306	(1,146)	(50%)
% of other digital engagement revenue	56%	60%		
Subtotal digital engagement services	10,231	10,114	117	1%
% of digital engagement services revenue	63%	54%		
Subscription and perpetual licenses	1,694	1,107	587	53%
% of subscription and perpetual licenses revenue	29%	28%		
Managed service hosting	280	317	(37)	(12%)
% of managed service hosting	*17*%	*17*%		
Total cost of revenue	12,205	11,538	667	6%
Gross profit	**11,532**	**12,968**	**(1,436)**	**(11%)**
Gross profit margin	**49%**	**53%**		
Operating expenses				
Sales and marketing	7,988	8,593	(605)	(7%)
% of total revenue	34%	35%		
General and administrative	4,392	4,474	(82)	(2%)
% of total revenue	19%	18%		
Research and development	2,386	1,365	1,021	75%
% of total revenue	10%	6%		
Depreciation and amortization	1,999	1,690	309	18%
% of total revenue	8%	7%		
Total operating expenses	**16,765**	**16,122**	**643**	**4%**

% of total revenue	71 %	66 %		
Loss from operations	(5,233)	(3,154)	(2,079)	66 %
Interest expense, net	(739)	(273)	(466)	171 %
Loss before income taxes	(5,972)	(3,427)	(2,545)	74 %
Provision for income taxes	243	171	72	42 %
Net loss	**$(6,215)**	**$(3,598)**	**$(2,617)**	**73 %**
Non-GAAP Measure				
Adjusted EBITDA	**$(2,241)**	**$(712)**	**$(1,529)**	**215 %**

Revenue

Our revenue is derived from three sources: (i) digital engagement services; (ii) subscription and perpetual licenses; and (iii) managed service hosting.

Digital Engagement Services

Digital engagement services revenue is comprised of iAPPS digital engagement services and other digital engagement services generated from non-iAPPS related engagements. Total revenue from digital engagement services decreased $2.2 million, or 12% to $16.4 million in fiscal 2014 from $18.6 million in fiscal 2013. The decrease in digital engagement services revenue compared to the prior period is due to an expected decrease in non-iAPPS digital engagement services revenues of $1.8 million, or 46% in fiscal 2014, when compared to fiscal 2013. Revenue from iAPPS related digital engagement services decreased $425 thousand, or 3% to $14.3 million compared to fiscal 2013. The decrease is attributable to an increase in iAPPSds related service revenues at lower margins as we expand this newer product line.

Digital engagement services revenue as a percentage of total revenue decreased to 69% in fiscal 2014 from 76% in fiscal 2013. The decrease is attributable to an increase in iAPPS license related revenue of 44% compared to prior year.

Subscription and Perpetual Licenses

Revenue from subscription and perpetual licenses increased $1.7 million, or 44%, to $5.7 million in fiscal 2014 from $4.0 million in fiscal 2013. Subscription and perpetual license revenue as a percentage of total revenue increased to 24% in fiscal 2014 from 16% in fiscal 2013.

The increases are due primarily to a higher amount of subscription license revenues from our iAPPSds product for multi-unit organizations and the franchise industry, annual maintenance renewals, and incremental SaaS license revenue from our acquisition of ElementsLocal (acquired in the fourth quarter of fiscal 2013).

Managed Service Hosting

Revenue from managed service hosting decreased $302 thousand, or 16%, to $1.6 million in fiscal 2014 from $1.9 million in fiscal 2013. The decreases are due to the ending of engagements with smaller hosting customers obtained through previous acquisitions. Managed services revenue as a percentage of total revenue was 7% in fiscal 2014 down from 8% in fiscal 2013.

The decreases are due to our efforts to engage with customers that are aligned with our core competencies and proactively end engagements with a number of smaller hosting customers obtained through previous acquisitions.

Cost of Revenue

Total cost of revenue for the fiscal year ended September 30, 2014 increased $667 thousand, or 6%, to $12.2 million from $11.5 million in fiscal 2013.

Cost of Digital Engagement Services

Cost of digital engagement services increased $117 thousand, or 1%, compared to fiscal 2013. The cost of total digital engagement services as a percentage of total digital engagement services revenue increased to 63% from 54% in fiscal 2013.

Cost of iAPPS digital engagement services increased $1.3 million, or 16%, to $9.1 million in fiscal 2014 from $7.8 million in fiscal 2013. Cost of iAPPS digital engagement services as a percentage of iAPPS digital engagement revenue increased to 63% from 53%. The increase is attributable to an increase in iAPPSds related service revenues at lower margins as we expand this newer product line.

Cost of other digital engagement services for fiscal 2014 decreased $1.1 million to $1.2 million in fiscal 2014, a decrease of 50% when compared to fiscal 2013. The decrease is due to reducing costs in line with non-iAPPS revenue decrease of 46%. The cost of other digital engagement services as a percentage of other digital enagagement service revenue decreased to 56% in fiscal 2014 from 60% in fiscal 2013.

Cost of Subscription and Perpetual License

Cost of subscription and perpetual licenses increased $587 thousand or 53% to $1.7 million in fiscal 2014 compared to $1.1 million in fiscal 2013. The cost of subscription and perpetual licenses as a percentage of subscription and perpetual license revenue increased to 29% in fiscal 2014 from 28% in fiscal 2013.

The increases are primarily due to costs to support our network operations center, amortization of software costs associated with the development of our iAPPS product, and incremental costs associated with the acquisition of ElementsLocal for a full year in fiscal 2014 compared to two months for fiscal 2013. These costs help support a 44% increase in subscription and perpetual license revenue in fiscal 2014.

Cost of Managed Service Hosting

Cost of managed service hosting decreased $37 thousand or 12% in fiscal 2014 to $280 thousand compared to $317 thousand in fiscal 2013. The decrease in the amount of managed service hosting costs is due to efforts to streamline costs by ending engagements with non-iAPPS related customers, and our continued investments in our co-managed network operation center to support our core iAPPS customer base. This decrease was due to managed service hosting revenue from low margin hosting customers decreasing faster than the addition of new, iAPPS related managed service hosting agreements for perpetual licenses. The cost of managed services as a percentage of managed services revenue was 17% for both periods.

Gross Profit

Gross profit decreased $1.4 million, or 11% in fiscal 2014 to $11.5 million compared to $13.0 million in fiscal 2013. The decrease is primarily attributable to the decrease in non-iAPPS related digital engagement revenue of 46%, as well as the iAPPSds engagements sold at lower margins due to the ramp up of this product line.

Operating Expenses

Sales and Marketing Expenses

Sales and marketing expenses decreased $605 thousand, or 7% to $8.0 million in fiscal 2014 from $8.6 million in fiscal 2013. Sales and marketing expense as a percentage of total revenue decreased to 34% in fiscal 2014 compared to 35% in fiscal 2013. The decreases are primarily attributable to decreases in compensation related expenses.

General and Administrative Expenses

General and administrative expenses decreased $82 thousand, or 2% to $4.4 million in fiscal 2014 from $4.5 million in fiscal 2013. The decrease is attributable to decreases in compensation and legal expenses. General and administrative expense as a percentage of revenue increased to 19% compared to 18% in fiscal 2013. The increase is due to fixed administrative costs required to support the revenue base.

Research and Development

Research and development expense increased by $1.0 million, or 75% to $2.4 million in fiscal 2014 from $1.4 million in fiscal 2013. Research and development expense as a percentage of total revenue increased to 10% in fiscal 2014 compared to 6% in fiscal 2013.

The increases are due to $486 thousand less in capitalized software development costs, as costs capitalized were $154 thousand and $640 thousand for fiscal 2014 and 2013, respectively. We capitalize development costs once technological feasibility has been established. Also, contributing to the increase in research and development costs are increases in compensation costs for additional headcount to support the expansion of the iAPPSds platform.

Depreciation and Amortization

Depreciation and amortization expense increased by $309 thousand, or 18% to $2.0 million in fiscal 2014 from $1.7 million in fiscal 2013. This increase is primarily attributable to additional depreciation expense related to investments made in our co-managed network operation center. Depreciation and amortization as a percentage of total revenue increased to 8% in fiscal 2014 from 7% in fiscal 2013.

Loss from Operations

The loss from operations was ($5.2) million for fiscal 2014 compared to a loss from operations of ($3.2) million for fiscal 2013. The increase in loss from operations is a result of the decrease in non-iAPPS related digital engagement services revenue and increases in research and development expenses for development of future products and enhancements.

Provision for Income Taxes

The provision for income tax expense was $243 thousand for fiscal 2014 compared to $171 thousand for fiscal 2013. The increase was attributable to non-deductible foreign withholding taxes. Income tax expense represents the estimated liability for Federal, state and foreign income taxes owed by the Company, including the alternative minimum tax. This increase is due to deferred tax liabilities related to indefinite lived, tax deductible assets from two previous acquisitions. The Company has net operating loss carryforwards and other deferred tax benefits that are available to offset future taxable income. A valuation allowance is established if it is more likely than not that all or a portion of the deferred tax asset will not be realized. Accordingly, the Company has established a full valuation allowance against its net deferred tax assets at September 30, 2014 and 2013.

The Federal net operating loss (NOL) carryforward of approximately $13.0 million as of September 30, 2014 expires on various dates through 2034. Internal Revenue Code Section 382 places a limitation on the amount of taxable income which can be offset by NOL carryforwards after a change in control of a loss corporation. Generally, after a change in control, a loss corporation cannot deduct NOL carryforwards in excess of the Section 382 Limitation. Due to these “change of ownership” provisions, utilization of NOL carryforwards may be subject to an annual limitation regarding their utilization against taxable income in future periods. The Company has not performed a Section 382 analysis. However, if performed, Section 382 may be found to limit potential future utilization of our NOL carryforwards.

Adjusted EBITDA

We also measure our performance based on a non-GAAP ("Generally Accepted Accounting Principles") measurement of earnings before interest, taxes, depreciation, and amortization and before stock-based compensation expense and impairment of goodwill and intangible assets ("Adjusted EBITDA").

We believe this non-GAAP financial measure of Adjusted EBITDA is useful to management and investors in evaluating our operating performance for the periods presented and provides a tool for evaluating our ongoing operations. Adjusted EBITDA, however, is not a measure of operating performance under GAAP and should not be considered as an alternative or substitute for GAAP profitability measures such as (i) income from operations and net income, or (ii) cash flows from operating, investing and financing activities, both as determined in accordance with GAAP. Adjusted EBITDA as an operating performance measure has material limitations since it excludes the financial statement impact of income taxes, net interest expense, amortization of intangibles, depreciation, other amortization and stock-based compensation, and therefore does not represent an accurate measure of profitability. As a result, Adjusted EBITDA should be evaluated in conjunction with net income for a complete analysis of our profitability, as net income includes the financial statement impact of these items and is the most directly comparable GAAP operating performance measure to Adjusted EBITDA. Our definition of Adjusted EBITDA may also differ from and therefore may not be comparable with similarly titled measures used by other companies, thereby limiting its usefulness as a comparative measure. Because of the limitations that Adjusted EBITDA has as an analytical tool, investors should not consider it in isolation, or as a substitute for analysis of our operating results as reported under GAAP.

The following table reconciles net loss (which is the most directly comparable GAAP operating performance measure) to EBITDA, and EBITDA to Adjusted EBITDA:

	Year Ended September 30,	
	2014	2013
Net loss	$(6,215)	$(3,598)
Provision for income taxes	243	171
Interest expense, net	739	273
Amortization of intangible assets	655	511
Depreciation	1,282	1,179
EBITDA	(3,296)	(1,464)
Other amortization	549	314
Stock-based compensation	506	438
Adjusted EBITDA	$(2,241)	$(712)

Adjusted EBITDA was ($2.2) million for fiscal 2014 compared with ($712) thousand for fiscal 2013. This was due to the decrease in non-iAPPS related digital engagement revenue compared to fiscal 2013.

Liquidity and Capital Resources

Cash Flows

Operating Activities

Cash used in operating activities was $3.8 million for fiscal 2014, compared to cash used in operating activities of $77 thousand for fiscal 2013. This decrease in cash from operating activities is primarily attributable to higher net loss for fiscal 2014 and decreases in accounts payables and accrued liabilities.

Investing Activities

Cash used in investing activities was $1.1 million for fiscal 2014 compared to $2.3 million for fiscal 2013. The decrease was primarily due to less purchases of capital equipment in fiscal 2014 than fiscal 2013 and less software development costs capitalized in fiscal 2014. Also contributing to the decrease in funds used for investing was a decrease in acquisition costs, as there were no acquisitions in fiscal 2014.

Financing Activities

Cash provided by financing activities was $3.6 million for fiscal 2014 compared with $3.0 million for fiscal 2013. The increase was due to the net proceeds from the sale of common stock and net borrowings on our line of credit. At September 30, 2014, the Company had an outstanding balance under its credit line with BridgeBank of $2.9 million and a short term loan of $1.0 million payable in full in October 2014.

Capital Resources and Liquidity Outlook

In December 2013, we entered into a Loan and Security Agreement with BridgeBank (the “BridgeBank Loan Agreement”). The BridgeBank Loan Agreement replaced the Company’s prior credit facility with Silicon Valley Bank (“SVB”), which expired on December 31, 2013. (See below) The Loan Agreement has a 27 month term which expires on March 31, 2016. The Loan Agreement provides for up to $5 million of revolving credit advances which may be used for acquisitions and working capital purposes. Borrowings are limited to the lesser of (i) $5 million and (ii) 80% of eligible receivables as defined. We can borrow up to $1.0 million in out of formula borrowings for specified periods of time. Borrowings bear interest at BridgeBank’s prime plus 1.00%. We pay an annual commitment fee of 0.25%. Borrowings are secured by all of the Company’s assets and all of the Company’s intellectual property. We are also required to comply with certain financial and reporting covenants including an Asset Coverage Ratio. As of September 30, 2014, we had an outstanding balance under the BridgeBank Loan Agreement of $2.9 million. We were in compliance with all reporting covenants for the period ended September 30, 2014, except for certain financial covenants, for which we obtained a waiver from BridgeBank. In December 2014, we amended the BridgeBank Loan Agreement which granted us a waiver for the covenants that we were not in compliance with and also modified the covenants prospectively. This amendment also added a personal guarantee from a stockholder/director for the out of formula borrowings up to $1.0 million.

On September 30, 2013, we entered into a Note Purchase Agreement (the "Purchase Agreement") with accredited investors pursuant to which Bridgeline Digital sold an aggregate of $2.0 million of 10% secured subordinated convertible notes (the "Notes"). The gross proceeds to Bridgeline Digital at the closing of this private placement were $2.0 million. The Notes accrue interest at a rate of ten percent (10%) per annum and mature on September 30, 2016. Interest on the Notes is payable quarterly in cash. The Notes are convertible at the election of the holder into shares of common stock of Bridgeline Digital at a conversion price equal to $1.30 per share at any time prior to the maturity date, provided that no holder may convert the Notes if such conversion would result in the holder beneficially owning more than 4.99% of the number of shares of Bridgeline Digital common stock outstanding at the time of conversion.

On November 6, 2013, we entered into an amendment (the "Amendment") to the Purchase Agreement by and among Bridgeline Digital and the accredited investors' party thereto. The Amendment increased the aggregate amount of 10% secured subordinated convertible notes (the "New Notes") able to be sold by Bridgeline Digital to $3.0 million. On November 6, 2013, Bridgeline Digital sold an additional $1.0 million of New Notes (the "Second Closing"). The gross proceeds to Bridgeline Digital at the Second Closing of this private placement were $1.0 million. The Notes accrue interest at a rate of ten percent (10%) per annum and mature on November 6, 2016. Interest on the Notes is payable quarterly in cash. The Notes are convertible at the election of the holder into shares of common stock of Bridgeline Digital at a conversion price equal to $1.30 per share at any time prior to the maturity date, provided that no holder may convert the Notes if such conversion would result in the holder beneficially owning more than 4.99% of the number of shares of Bridgeline Digital common stock outstanding at the time of conversion.

The Notes are secured by all of Bridgeline Digital's assets. The security interest granted to the holders of the Notes is subordinate to the security interest held by Bridgeline Digital's senior lender, BridgeBank. Bridgeline Digital may prepay any portion of the principal amount of the outstanding Notes at any time, provided that if Bridgeline Digital prepays any principal on or before September 30, 2014, Bridgeline Digital will pay a penalty equal to 10% of the principal amount being prepaid. Under certain circumstances Bridgeline Digital has the right to force conversion of the Notes into shares of Bridgeline Digital common stock in the event the Bridgeline Digital common stock trades in excess of $2.60 per share for 20 trading days out of any 30 trading day period.

The Notes contain customary events of default. Upon the occurrence of any event of default the interest rate under the Notes will increase. In addition, upon the occurrence of a payment default under the Notes, Bridgeline Digital must pay a premium equal to 20% of the outstanding principal amount of the Notes. In the event of a change in control of Bridgeline Digital while the Notes are outstanding, Bridgeline Digital will provide the holders of the Notes with the opportunity to convert the Notes immediately prior to the change in control. In the event the holders of the Notes do not elect to convert the Notes, Bridgeline Digital may prepay all outstanding principal and accrued interest under the Notes.

In May 2012, we assumed two Promissory Notes in connection with the acquisition of MarketNet, Inc. The first Promissory Note in the amount of $63 thousand matured in May 2014 and was paid in full. The second Promissory Note in the amount of $80 thousand is payable in twelve equal installments of $7 thousand, including interest accrued at 5%, and matures in May 2015. The balance due on this Promissory Note as of September 30, 2014 is $21 thousand.

On October 27, 2014, we sold 200,000 shares of convertible preferred stock (the “Preferred Stock”) at a purchase price of $10.00 per share for gross proceeds of $2.0 million in a private placement. Net proceeds to the Company after offering expenses were approximately $1.8 million. Each share of Preferred Stock will be convertible into shares of common stock at a conversion price of $0.65 per share. Cumulative dividends are payable in cash quarterly at a rate of 6% per year. If we do not pay the dividends in cash, then we may pay dividends in any quarter by delivery of additional shares of Preferred Stock (“PIK Election”). If we make the PIK Election with respect to the dividend payable, it shall deliver a number of shares of Preferred Stock equal to (A) the aggregate dividend payable to such holder as of the end of the quarter divided by (B) the lesser of (x) the then effective Conversion Price or (y) the average VWAP for the five (5) consecutive Trading Days prior to such dividend payment date. If, after two years, any Preferred Stock are outstanding the cash dividend rate will increase to 12.0% per year. We shall have the right to force conversion of the Preferred Stock into shares of Common Stock at any time after the Common Stock trades in excess of $1.30 per share. The Preferred Shares shall vote with the Common an as converted basis.

We believe that cash generated from operations and proceeds from the bank line of credit, the sale of common stock and sale of preferred stock will be sufficient to fund the Company’s working capital and capital expenditure needs in the foreseeable future. However, we currently have a borrowing facility with Bridge Bank from which we can borrow, and this line is subject to financial covenants that must be met. It is not certain that all or part of this line will be available to us in the future; and other sources of financing may not be available to us in a timely basis if at all, or on terms acceptable to us. If we fail to obtain acceptable funding when needed, we may not have sufficient resources to fund our normal operations, and this would have a material adverse effect on our business.

Inflation

Inflationary increases can cause pressure on wages and the cost of benefits offered to employees. We believe that the relatively moderate rates of inflation in recent years have not had a significant impact on our operations.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, financings or other relationships with unconsolidated entities or other persons, other than our operating leases and contingent acquisition payments.

We currently do not have any variable interest entities. We do not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Therefore, we are not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

Contractual Obligations

We lease our facilities in the United States and India. Other contractual obligations include: (i) certain equipment acquired under capitalized lease agreements; (ii) a subordinated promissory note with a balance due of $21 thousand which matures in 2015; (iii) contingent earnouts in the amount of $868 thousand payable in cash on the achievement of revenue and earnings targets; (iv) a short term bank loan of $1.0 million due in October 2014; and (v) subordinated convertible debt of $3.0 million due in 2016.

The following summarizes our contractual obligations:

	For the Year Ending September 30,					
(in thousands)	**2015**	**2016**	**2017**	**2018**	**2019 and thereafter**	**Total**
Payment obligations by year						
Line of credit	$-	$2,938	$-	$-	$ -	$2,938
Subordinated convertible debt	-	2,000	1,000	-	-	3,000
Short term bank loan (a)	1,000	-	-	-	-	1,000
Subordinated promissory notes	21	-	-	-	-	21
Capital leases	364	247	-	-	-	611
Operating leases (b)	1,342	1,265	999	905	504	5,015
Contingent acquisition payments (c)	487	301	80	-	-	868
Total	$3,214	$6,751	$2,079	$905	$ 504	$13,453

(a) Paid in full in October 2014.
(b) Net of sublease income.
(c) The contingent acquisition payments are maximum potential earn-out consideration payable to former owners of acquired companies. Amounts actually paid may be less. Contingent acquisition payments do not include $0.6 million of potential common stock issuable upon achievement of certain revenue and earnings targets.

Critical Accounting Policies

These critical accounting policies and estimates by our management should be read in conjunction with Note 2 *Summary of Significant Accounting Policies* to the Consolidated Financial Statements that were prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

The preparation of financial statements in accordance US GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses in the reporting period. We regularly make estimates and assumptions that affect the reported amounts of assets and liabilities. The most significant estimates included in our financial statements are the valuation of accounts receivable and long-term assets, including intangibles, goodwill and deferred tax assets, stock-based compensation, amounts of revenue to be recognized on service contracts in progress, unbilled receivables, and deferred revenue. We base our estimates and assumptions on current facts, historical experience and various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities and the accrual of costs and expenses that are not readily apparent from other sources. The actual results experienced by us may differ materially and adversely from our estimates. To the extent there are material differences between our estimates and the actual results, our future results of operations will be affected.

We consider the following accounting policies to be both those most important to the portrayal of our financial condition and those that require the most subjective judgment:

- Revenue recognition;
- Allowance for doubtful accounts;
- Accounting for cost of computer software to be sold, leased or otherwise marketed;
- Accounting for goodwill and other intangible assets; and
- Accounting for stock-based compensation.

Revenue Recognition

Overview

We enter into arrangements to sell digital engagement services (professional services), software licenses or combinations thereof. Revenue is categorized into (i) digital engagement services; (ii) managed service hosting; and (iii) subscriptions and perpetual licenses.

We recognize revenue as required by the *Revenue Recognition* Topic of the Codification. Revenue is generally recognized when all of the following conditions are satisfied: (1) there is persuasive evidence of an arrangement; (2) delivery has occurred or the services have been provided to the customer; (3) the amount of fees to be paid by the customer is fixed or determinable; and (4) the collection of the fees is reasonably assured. Billings made or payments received in advance of providing services are deferred until the period these services are provided.

We maintain a reseller channel to supplement our direct sales force for our iAPPS platform. Resellers are generally located in territories where we do not have a direct sales force. Customers generally sign a license agreement directly with us. Revenue from perpetual licenses sold through resellers is recognized upon delivery to the end user as long as evidence of an arrangement exists, collectability is probable, and the fee is fixed and determinable. Revenue for subscription licenses is recognized monthly as the services are delivered.

Digital Engagement Services

Digital engagement services include professional services primarily related to the Company’s web development solutions that address specific customer needs such as digital strategy, information architecture and usability engineering, .Net development, rich media development, back end integration, search engine optimization, quality assurance and project management.

Digital engagement services are contracted for on either a fixed price or time and materials basis. For its fixed price engagements, after assigning the relative selling price to the elements of the arrangement, the Company applies the proportional performance model (if not subject to contract accounting) to recognize revenue based on cost incurred in relation to total estimated cost at completion. The Company has determined that labor costs are the most appropriate measure to allocate revenue among reporting periods, as they are the primary input when providing application development services. Customers are invoiced monthly or upon the completion of milestones. For milestone based projects, since milestone pricing is based on expected hourly costs and the duration of such engagements is relatively short, this input approach principally mirrors an output approach under the proportional performance model for revenue recognition on such fixed priced engagements. For time and materials contracts, revenues are recognized as the services are provided.

Digital engagement services also include retained professional services contracted for on an "on call" basis or for a certain amount of hours each month. Such arrangements generally provide for a guaranteed availability of a number of professional services hours each month on a "use it or lose it" basis. For retained professional services sold on a stand-alone basis we recognize revenue as the services are delivered or over the term of the contractual retainer period. These arrangements do not require formal customer acceptance and do not grant any future right to labor hours contracted for but not used.

Subscriptions and Perpetual Licenses

The Company licenses its software on either a perpetual or subscription basis. Customers who license the software on a perpetual basis receive rights to use the software for an indefinite time period and an option to purchase Post-Customer Support ("PCS"). For arrangements that consist of a perpetual license and PCS, as long as Vendor Specific Objective Evidence ("VSOE") exists for the PCS, then PCS revenue is recognized ratably on a straight-line basis over the period of performance and the perpetual license is recognized on a residual basis. Under the residual method, the fair value of the undelivered elements are deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and recognized as revenue, assuming all other revenue recognition criteria have been met.

Customers may also license the software on a subscription basis, which can be described as "Software as a Service" or "SaaS". SaaS is a model of software deployment where an application is hosted as a service provided to customers across the Internet. Subscription agreements include access to the Company's software application via an internet connection, the related hosting of the application, and PCS. Customers receive automatic updates and upgrades, and new releases of the products as soon as they become available. Customers cannot take possession of the software. Subscription agreements are either annual or month-to-month arrangements that provide for termination for convenience by either party upon 90 days notice. Revenue is recognized monthly as the services are delivered. Set up fees paid by customers in connection with subscription services are deferred and recognized ratably over the longer of the life of subscription period or the expected lives of customer relationships. We continue to evaluate the length of the amortization period of the set up fees as we gain more experience with customer contract renewals.

Managed Service Hosting

Managed service hosting includes hosting arrangements that provide for the use of certain hardware and infrastructure for those customers who do not wish to host our applications independently. Hosting agreements are either annual or month-to-month arrangements that provide for termination for convenience by either party generally upon 30-days notice. Revenue is recognized monthly as the hosting services are delivered. Set up fees paid by customers in connection with managed hosting services are deferred and recognized ratably over the longer of the life of the hosting period or the expected lives of customer relationships. We continue to evaluate the length of the amortization period of the set up fees as we gain more experience with customer contract renewals.

Multiple Element Arrangements

In accounting for multiple element arrangements, we follow either ASC Topic 605-985 *Revenue Recognition Software* or ASC Topic 605-25 *Revenue Recognition Multiple Element Arrangements*, as applicable.

In October 2009, the FASB issued Accounting Standards Update No. 2009-13, *Revenue Recognition: Multiple-Deliverable Revenue Arrangements* (“ASU 2009-13”). ASU 2009-13 provides amendments to certain paragraphs of previously issued ASC Subtopic 605-25 – *Revenue Recognition: Multiple-Deliverable Revenue Arrangements*. In accordance with ASU 2009-13, each deliverable within a multiple-deliverable revenue arrangement is accounted for as a separate unit of accounting if both of the following criteria are met (1) the delivered item has value to the customer on a standalone basis and (2) for an arrangement that includes a right of return relative to the delivered item, delivery or performance of the delivered item is considered probable and within our control. If the deliverables do not meet the criteria for being a separate unit of accounting then they are combined with a deliverable that does meet that criterion. The accounting guidance also requires that arrangement consideration be allocated at the inception of an arrangement to all deliverables using the relative selling price method. The accounting guidance also establishes a selling price hierarchy for determining the selling price of a deliverable. We determine selling price using VSOE, if it exists; otherwise, we use Third-party Evidence (“TPE”). If neither VSOE nor TPE of selling price exists for a unit of accounting, we use Estimated Selling Price (“ESP”).

VSOE is generally limited to the price at which we sell the element in a separate stand-alone transaction. TPE is determined based on the prices charged by our competitors for a similar deliverable when sold separately. It is difficult for us to obtain sufficient information on competitor pricing, so we may not be able to substantiate TPE. If we cannot establish selling price based on VSOE or TPE then we will use ESP. ESP is derived by considering the selling price for similar services and our ongoing pricing strategies. The selling prices used in our allocations of arrangement consideration are analyzed at minimum on an annual basis and more frequently if our business necessitates a more timely review. We have determined that we have VSOE on our SaaS offerings, certain application development services, managed hosting services, and PCS because we have evidence of these elements sold on a stand-alone basis.

When the Company licenses its software on a perpetual basis in a multiple element arrangement that arrangement typically includes PCS and application development services, we follow the guidance of ASC Topic 605-985. In assessing the hierarchy of relative selling price for PCS, we have determined that VSOE is established for PCS. VSOE for PCS is based on the price of PCS when sold separately, which has been established via annual renewal rates. Similarly, when the Company licenses its software on a perpetual basis in a multiple element arrangement that also includes managed service hosting (“hosting”), we have determined that VSOE is established for hosting based on the price of the hosting when sold separately, which has been established based on renewal rates of the hosting contract. Revenue recognition for perpetual licenses sold with application development services are considered on a case by case basis. The Company has not established VSOE for perpetual licenses or fixed price development services and therefore in accordance with ASC Topic 605-985, when perpetual licenses are sold in multiple element arrangements including application development services where VSOE for the services has not been established, the license revenue is deferred and recognized using contract accounting. The Company has determined that services are not essential to the functionality of the software and it has the ability to make estimates necessary to apply proportional performance model. In those cases where perpetual licenses are sold in a multiple element arrangement that includes application development services where VSOE for the services has been established, the license revenue is recognized under the residual method and the application services are recognized upon delivery.

In determining VSOE for the digital engagement services element, the separability of the services from the software license and the value of the services when sold on a standalone basis are considered. The Company also considers the categorization of the services, the timing of when the services contract was signed in relation to the signing of the perpetual license contract and delivery of the software, and whether the services can be performed by others. The Company has concluded that its application development services are not required for the customer to use the product but, rather enhance the benefits that the software can bring to the customer. In addition, the services provided do not result in significant customization or modification of the software and are not essential to its functionality, and can also be performed by the customer or a third party. If an application development services arrangement does qualify for separate accounting, the Company recognizes the perpetual license on a residual basis. If an application development services arrangement does not qualify for separate accounting, the Company recognizes the perpetual license under the proportional performance model as described above.

When subscription arrangements are sold with application development services, the Company uses its judgment as to whether the application development services qualify as a separate unit of accounting. When subscription service arrangements involve multiple elements that qualify as separate units of accounting, the Company allocates arrangement consideration in multiple-deliverable arrangements at the inception of an arrangement to all deliverables based on the relative selling price model in accordance with the selling price hierarchy, which includes: (i) VSOE when available; (ii) TPE if VSOE is not available; and (iii) ESP if neither VSOE or TPE is available. For those subscription arrangements sold with multiple elements whereby the application development services do not qualify as a separate unit of accounting, the application services revenue is recognized ratably over the subscription period. Subscriptions also include a PCS component, and the Company has determined that the two elements cannot be separated and must be recognized as one unit over the applicable service period. Set up fees paid by customers in connection with subscription arrangements are deferred and recognized ratably over the longer of the life of the hosting period or the expected lives of customer relationships, which generally range from two to three years. We continue to evaluate the length of the amortization period of the set up fees as we gain more experience with customer contract renewals and our newer product offerings.

Customer Payment Terms

Payment terms with customers typically require payment 30 days from invoice date. Payment terms may vary by customer but generally do not exceed 45 days from invoice date. Invoicing for digital engagement services are either monthly or upon achievement of milestones and payment terms for such billings are within the standard terms described above. Invoicing for subscriptions and hosting are typically issued monthly and are generally due in the month of service. The Company’s subscription and hosting agreements provide for refunds when service is interrupted for an extended period of time and are reserved for in the month in which they occur if necessary.

Our digital engagement services agreements with customers do not provide for any refunds for services or products and therefore no specific reserve for such is maintained. In the infrequent instances where customers raise a concern over delivered products or services, we have endeavored to remedy the concern and all costs related to such matters have been insignificant in all periods presented.

Warranty

Certain arrangements include a warranty period, which is generally 30 days from the completion of work. In hosting arrangements, we provide warranties of up-time reliability. We continue to monitor the conditions that are subject to the warranties to identify if a warranty claim may arise. If we determine that a warranty claim is probable, then any related cost to satisfy the warranty obligation is estimated and accrued. Warranty claims to date have been immaterial.

Reimbursable Expenses

In connection with certain arrangements, reimbursable expenses are incurred and billed to customers and such amounts are recognized as both revenue and cost of revenue.

Allowance for Doubtful Accounts

We maintain an allowance for doubtful accounts which represents estimated losses resulting from the inability, failure or refusal of our clients to make required payments.

We analyze historical percentages of uncollectible accounts and changes in payment history when evaluating the adequacy of the allowance for doubtful accounts. We use an internal collection effort, which may include our sales and services groups as we deem appropriate. Although we believe that our allowances are adequate, if the financial condition of our clients deteriorates, resulting in an impairment of their ability to make payments, or if we underestimate the allowances required, additional allowances may be necessary, resulting in increased expense in the period in which such determination is made.

Accounting for Cost of Computer Software to be Sold, Leased or Otherwise Marketed

We charge research and development expenditures for technology development to operations as incurred. However, in accordance with Codification 985-20 *Costs of Software to be Sold Leased or Otherwise Marketed*, we capitalize certain software development costs subsequent to the establishment of technological feasibility. Based on our product development process, technological feasibility is established upon completion of a working model. Certain costs incurred between completion of a working model and the point at which the product is ready for general release is capitalized if significant. Once the product is available for general release, the capitalized costs are amortized in cost of sales.

Accounting for Goodwill and Intangible Assets

Goodwill is tested for impairment annually during the fourth quarter of every year and more frequently if events and circumstances indicate that the asset might be impaired. In assessing goodwill for impairment, an entity has the option to assess qualitative factors to determine whether events or circumstances indicate that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount. We assess goodwill at the consolidated level as one reporting unit. If this is the case, then performing the quantitative two-step goodwill impairment test is unnecessary. An entity can choose not to perform a qualitative assessment for any or all of its reporting units, and proceed directly to the use of the two-step impairment test. In assessing qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we assess relevant events and circumstances that may impact the fair value and the carrying amount of a reporting unit. The identification of relevant events and circumstances and how these may impact a reporting unit's fair value or carrying amount involve significant judgments by management. These judgments include the consideration of macroeconomic conditions, industry and market considerations, cost factors, overall financial performance, events which are specific to Bridgeline, and trends in the market price of our common stock. Each factor is assessed to determine whether it impacts the impairment test positively or negatively, and the magnitude of any such impact.

For fiscal 2014, we performed the annual assessment of our goodwill during the fourth quarter of 2014, using the qualitative approach described above. Based on our qualitative assessment, we concluded that it was not more likely than not that the fair values of any of our reporting units were less than their carrying amounts, and therefore it was not necessary to perform the quantitative two-step impairment test. The key qualitative factors that led to our conclusion included the following: (i) Positive access to capital with two recent stock offerings totaling $5 million in capital; (ii) Positive market acceptance of our multi-unit products; and (iii) Fair market value of Company is in excess of book value.

For fiscal 2013, we performed the annual assessment of our goodwill during the fourth quarter of 2013, using the qualitative approach described above. Based on our qualitative assessment, we concluded that it was not more likely than not that the fair values of any of our reporting units were less than their carrying amounts, and therefore it was not necessary to perform the quantitative two-step impairment test. The key qualitative factors that led to our conclusion included the following: (i) our stock price of $1.10 as of September 30, 2013 did not materially change from the stock price of $1.20 of September 30, 2012; (ii) the successful launch of iAPPSds in 2012 with our first iAPPSds customer, a franchisor with over 4,000 locations, and our strategic acquisition of ElementsLocal in 2013, has improved predictability of our forecasts by increasing contractually recurring revenue; and (iii) inputs from recent transactions within the technology sector, such as revenue multiples used to value transactions, have either remained steady since the fiscal 2012 assessment.

Accounting for Stock-Based Compensation

At September 30, 2014, we maintained one stock-based compensation plan more fully described in Note 12.

The Company accounts for stock-based compensation awards in accordance with the *Compensation-Stock* Topic of the Codification. Share-based payments (to the extent they are compensatory) are recognized in our consolidated statements of operations based on their fair values.

We recognize stock-based compensation expense for share-based payments issued or assumed after October 1, 2006 that are expected to vest on a straight-line basis over the service period of the award, which is generally three years. We recognize the fair value of the unvested portion of share-based payments granted prior to October 1, 2006 over the remaining service period, net of estimated forfeitures. In determining whether an award is expected to vest, we use an estimated, forward-looking forfeiture rate based upon our historical forfeiture rate and reduce the expense over the recognition period. Estimated forfeiture rates are updated for actual forfeitures quarterly. We also consider, each quarter, whether there have been any significant changes in facts and circumstances that would affect our forfeiture rate. Although we estimate forfeitures based on historical experience, actual forfeitures in the future may differ. In addition, to the extent our actual forfeitures are different than our estimates, we record a true-up for the difference in the period that the awards vest, and such true-ups could materially affect our operating results.

We estimate the fair value of employee stock options using the Black-Scholes-Merton option valuation model. The fair value of an award is affected by our stock price on the date of grant as well as other assumptions including the estimated volatility of our stock price over the term of the awards and the estimated period of time that we expect employees to hold their stock options. The risk-free interest rate assumption we use is based upon United States treasury interest rates appropriate for the expected life of the awards. We use the historical volatility of our publicly traded options in order to estimate future stock price trends. In order to determine the estimated period of time that we expect employees to hold their stock options, we use historical trends of employee turnovers. Our expected dividend rate is zero since we do not currently pay cash dividends on our common stock and do not anticipate doing so in the foreseeable future. The aforementioned inputs entered into the option valuation model we use to fair value our stock awards are subjective estimates and changes to these estimates will cause the fair value of our stock awards and related stock-based compensation expense we record to vary.

We record deferred tax assets for stock-based awards that result in deductions on our income tax returns, based on the amount of stock-based compensation recognized and the statutory tax rate in the jurisdiction in which we will receive a tax deduction.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Not required.

Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

To the Board of Directors of

Bridgeline Digital, Inc.

Burlington, MA.:

We have audited the consolidated balance sheets of Bridgeline Digital, Inc., and subsidiaries (the "Company") as of September 30, 2014 and 2013, and the related consolidated statements of operations, comprehensive loss, stockholders' equity and cash flows for each of the years in the period then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Bridgeline Digital, Inc. as of September 30, 2014 and 2013, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ Marcum LLP

Marcum LLP

December 29, 2014

Boston, Massachusetts

BRIDGELINE DIGITAL, INC.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share data)

	September 30, 2014	September 30, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$1,256	$2,830
Accounts receivable and unbilled receivables, net	3,342	3,194
Prepaid expenses and other current assets	747	963
Total current assets	5,345	6,987
Equipment and improvements, net	2,175	3,065
Intangible assets, net	1,582	1,517
Goodwill	23,141	23,777
Other assets	1,317	1,631
Total assets	$33,560	$36,977
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$1,126	$1,746
Accrued liabilities	957	1,093
Accrued earnouts, current	487	561
Debt, current, net of unamortized debt discount	985	1,165
Capital lease obligations, current	364	397
Deferred revenue	1,990	1,960
Total current liabilities	5,909	6,922
Accrued earnouts, net of current portion	381	950
Debt, net of current portion, net of unamortized debt discount	5,935	4,725
Capital lease obligations, net of current portion	247	544
Other long term liabilities	1,155	1,088
Total liabilities	13,627	14,229
Commitments and contingencies (See note 11)		
Stockholders' equity:		
Preferred stock - $0.001 par value; 1,000,000 shares authorized; none issued and outstanding	-	-
Common stock - $0.001 par value; 50,000,000 shares authorized; 21,942,912 and 18,313,765 shares issued and outstanding, respectively	22	18
Additional paid-in capital	47,773	44,206

Accumulated deficit	(27,529)	(21,314)
Accumulated other comprehensive loss	(333)	(162)
Total stockholders' equity	19,933	22,748
Total liabilities and stockholders' equity	$33,560	$36,977

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

BRIDGELINE DIGITAL, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in thousands, except per share data)

	Years Ended September 30, 2014	2013
Revenue:		
Digital engagement services	$16,369	$18,585
Subscription and perpetual licenses	5,749	4,000
Managed service hosting	1,619	1,921
Total revenue	23,737	24,506
Cost of revenue:		
Digital engagement services	10,231	10,114
Subscription and perpetual licenses	1,694	1,107
Managed service hosting	280	317
Total cost of revenue	12,205	11,538
Gross profit	11,532	12,968
Operating expenses:		
Sales and marketing	7,988	8,593
General and administrative	4,392	4,474
Research and development	2,386	1,365
Depreciation and amortization	1,999	1,690
Impairment of intangible asset	-	-
Total operating expenses	16,765	16,122
Loss from operations	(5,233)	(3,154)
Interest expense, net	(712)	(273)
Other expense, net	(27)	-
Loss before income taxes	(5,972)	(3,427)
Provison for income taxes	243	171
Net loss	$(6,215)	$(3,598)
Net loss per share:		
Basic and diluted	$(0.32)	$(0.23)
Number of weighted average shares:		
Basic and diluted	19,689,930	15,558,244

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

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BRIDGELINE DIGITAL, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Dollars in thousands)

	Year Ended September 30,	
	2014	**2013**
Net Loss	$(6,215)	$(3,598)
Other Comprehensive Gain(Loss): Net change in foreign currency translation adjustment	(171)	14
Comprehensive loss	$(6,386)	$(3,584)

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

BRIDGELINE DIGITAL, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(Dollars in thousands)

	Common Stock		Additional		Accumulated Other	Total
	Shares	Par Value	Paid in Capital	Accumulated Deficit	Comprehensive Loss	Stockholders' Equity
Balance at September 30, 2012	15,209,038	$ 15	$ 40,847	$ (17,716)	$ (176)	$ 22,970
Issuance of common stock	2,300,000	3	2,044	-	-	2,047
Stock-based compensation	-	-	438	-	-	438
Issuance of common stock - ESPP	56,112	-	74	-	-	74
Issuance of common stock - Warrants	22,599	-	-	-	-	-
Issuance of common stock - acquisition	526,438	-	995	-	-	995
Decrease in estimate of contingent shares that will be earned from a prior acquisition	-	-	(354)	-	-	(354)
Exercise of stock options	199,578	-	162	-	-	162
Net loss	-	-	-	(3,598)	-	(3,598)
Foreign currency translation adjustment	-	-	-	-	14	14
Balance at September 30, 2013	18,313,765	18	44,206	(21,314)	(162)	22,748
Issuance of common stock	3,200,000	3	2,743	-	-	2,746
Stock-based compensation	-	-	449	-	-	449
Issuance of common stock - ESPP	26,548	-	22	-	-	22
Issuance of common stock - Contingent shares	84,615	-	-	-	-	-
Issuance of common stock - Restricted shares	56,898	-	66	-	-	66
Exercise of stock options	261,086	1	215	-	-	216
Fair value of warrants issued	-	-	72	-	-	72
Net loss	-	-	-	(6,215)	-	(6,215)
Foreign currency translation adjustment	-	-	-	-	(171)	(171)
Balance at September 30, 2014	21,942,912	$ 22	$ 47,773	$ (27,529)	$ (333)	$ 19,933

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

BRIDGELINE DIGITAL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

	Year Ended September 30, 2014	2013
Cash flows from operating activities:		
Net loss	$ (6,215)	$ (3,598)
Adjustments to reconcile net loss to net cash used in operating activities:		
Change in deferred taxes	219	102
Amortization of intangible assets	655	511
Depreciation	1,282	1,179
Other amortization	549	314
Stock-based compensation	506	437
Adjustments to accrued earnouts	(9)	(507)
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable and unbilled receivables	(162)	886
Prepaid expenses and other assets	899	160
Accounts payable and accrued liabilities	(1,414)	(192)
Deferred revenue	(6)	729
Other liabilities	(152)	(98)
Total adjustments	2,367	3,521
Net cash used in operating activities	(3,848)	(77)
Cash flows from investing activities:		
Equipment and improvements	(304)	(545)
Software development capitalization costs/other intangibles	(164)	(814)
Acquisitions, net of cash acquired	-	(364)
Contingent acquisition payments	(644)	(531)
Net cash used in investing activities	(1,112)	(2,254)
Cash flows from financing activities:		
Proceeds from sale of common stock, net of issuance costs	2,756	2,044
Proceeds from exercise of employee stock options	215	162
Proceeds from employee stock purchase plan	22	74
Proceeds from convertible debt, net of issuance costs	913	1,790
Borrowings from bank line of credit	2,046	1,092
Payments on term loan	-	(620)
Payments on bank line of credit	(1,884)	(769)
Payments on acquired debt	(42)	(188)
Payments on subordinated promissory notes	(51)	(225)
Principal payments on capital leases	(418)	(339)
Net cash provided by financing activities	3,557	3,021
Effect of exchange rate changes on cash and cash equivalents	(171)	14

Net (decrease) increase in cash and cash equivalents	(1,574)	704
Cash and cash equivalents at beginning of period	2,830	2,126
Cash and cash equivalents at end of period	$ 1,256	$2,830
Supplemental disclosures of cash flow information:		
Cash paid for:		
Interest	$ 245	$273
Income taxes	$ 57	$53
Non cash activities:		
Equipment and other assets included in accounts payable	-	$50
Equipment purchased under capital leases	$ 88	$855
Accrued contingent consideration (earnouts)	$ -	$906
Common stock issued in connection with acquisition	$ -	$604

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

BRIDGELINE DIGITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

1. Description of Business

Overview

Bridgeline Digital, The Digital Engagement Company™, enables its customers to maximize the performance of their mission critical websites, intranets, and online stores. Bridgeline's iAPPS® platform deeply integrates Web Content Management, eCommerce, eMarketing, Social Media management, and Web Analytics to help marketers deliver online experiences that attract, engage and convert their customers across all digital channels. Bridgeline's iAPPS platform combined with its digital services assists customers in maximizing on-line revenue, improving customer service and loyalty, enhancing employee knowledge, and reducing operational costs.

In fiscal 2012, Bridgeline Digital announced the release of iAPPSds ("distributed subscription"), a platform that empowers franchise and multi-unit organizations with state-of-the-art web engagement management while providing superior oversight of corporate branding. iAPPSds deeply integrates content management, eCommerce, eMarketing and web analytics and is a self-service web platform that is offered to each authorized franchise or dealer for a monthly subscription fee. On August 1, 2013, we acquired franchise web developer ElementsLocal, expanding Bridgeline Digital's presence in the franchise market place.

The iAPPS platform is delivered through a cloud-based SaaS ("Software as a Service") multi-tenant business model, whose flexible architecture provides customers with state of the art deployment providing maintenance, daily technical operation and support; or via a traditional perpetual licensing business model, in which the iAPPS software resides on a dedicated server in either the customer's facility or Bridgeline's co-managed hosting facility.

iAPPS Content Manager and iAPPS Commerce were selected as finalists for the 2014, 2013, and 2012 CODiE Awards for Best Content Management Solution and Best Electronic Commerce Solution, globally. In 2014, Bridgeline Digital won ten Horizon Interactive Awards for outstanding development of web applications and websites and won fifteen Horizon Interactive Awards in 2013. Also in 2013, the Web Marketing Association sponsored Internet Advertising Competition honored Bridgeline Digital with three awards for iAPPS customer websites and B2B Magazine selected Bridgeline Digital as one of the Top Interactive Technology companies in the United States. In 2013, KMWorld Magazine Editors selected Bridgeline Digital as one of the 100 Companies That Matter in Knowledge Management and also selected iAPPS as a Trend Setting Product in 2013.

Bridgeline Digital was incorporated under the laws of the State of Delaware on August 28, 2000.

Locations

The Company's corporate office is located north of Boston, Massachusetts. The Company maintains regional field offices serving the following geographical locations: Atlanta, GA; Baltimore, MD; Boston, MA; Chicago, IL; Denver, CO; New York, NY; Dallas, TX; San Diego, CA; San Luis Obispo, CA; and Tampa, FL. The Company has one wholly-owned subsidiary, Bridgeline Digital Pvt. Ltd. located in Bangalore, India.

Liquidity

The Company has incurred operating losses and used cash in its operating activities for the past several years. Cash was used to fund acquisitions to broaden our geographic footprint, develop new products, and build infrastructure, while also ramping down a lower margin services model. The Company is currently working on reducing operating expenses. The Company's management believes it will have an appropriate cost structure for its anticipated sales in the second half of fiscal 2015. Management believes that operating expenses will be reduced to the point where the Company can drive positive Adjusted EBITDA (earnings before interest, taxes, depreciation and amortization and stock-based compensation charges). As such, management believes that the Company will provide sufficient cash flows to fund its operations in the ordinary course of business through at least the next twelve months. However, there can be no assurance that the anticipated sales level will be achieved. The Company also maintains a bank financing agreement which provides for up to $5 million of revolving credit advances. Borrowing is limited to the lesser of the $5 million or 80% of eligible receivables. Additionally, the Company can borrow up to $1 million in out of formula borrowings, which are further guaranteed by a director/shareholder of the Company.

2. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant inter-company accounts and transactions have been eliminated in consolidation.

BRIDGELINE DIGITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported periods. The most significant estimates included in these financial statements are the valuation of accounts receivable and long-term assets, including intangibles, goodwill and deferred tax assets, stock-based compensation, amounts of revenue to be recognized on service contracts in progress, unbilled receivables, and deferred revenue. Actual results could differ from these estimates under different assumptions or conditions.

The complexity of the estimation process and factors relating to assumptions, risks and uncertainties inherent with the use of the proportional performance model affect the amount of revenue and related expenses reported in the Company's financial statements. Internal and external factors can affect the Company's estimates.

Cash and Cash Equivalents

The Company considers all highly liquid instruments with original maturity of three months or less from the date of purchase to be cash equivalents.

Concentration of Credit Risk, Significant Customers, and Off-Balance Sheet Risk

Financial instruments, which potentially expose the Company to concentrations of credit risk consist primarily of cash, cash equivalents, and accounts receivable. The Company's cash is maintained with what management believes to be a high-credit quality financial institution. At times, deposits held at this bank may exceed the federally insured limits. Management believes that the financial institutions that hold the Company's deposits are financially sound and have minimal credit risk. Risks associated with cash and cash equivalents are mitigated by the Company's investment policy, which limits the Company's investing of excess cash into only money market mutual funds.

The Company extends credit to customers on an unsecured basis in the normal course of business. Management performs ongoing credit evaluations of its customers' financial condition and limits the amount of credit when deemed necessary. Accounts receivable are carried at original invoice less an estimate for doubtful accounts based on a review of all outstanding amounts. The Company did not have any customers that contributed greater than 10% of revenue for the fiscal years ended September 30, 2014 ("fiscal 2014) and 2013 ("fiscal 2013"), respectively.

The Company has no significant off-balance sheets risks such as foreign exchange contracts, interest rate swaps, option contracts or other foreign hedging agreements.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. For all customers, the Company recognizes allowances for doubtful accounts based on the length of time that the receivables are past due, current business environment and its historical experience. If the financial condition of the Company's customers were to deteriorate, resulting in impairment of their ability to make payments, additional allowances may be required. The Company did not have any customers that had an accounts receivable balance of greater than 10% of total accounts receivable at September 30, 2014 and 2013.

BRIDGELINE DIGITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

Revenue Recognition

Overview

The Company enters into arrangements to sell digital engagement services (professional services), software licenses or combinations thereof. Revenue is categorized into: (i) Digital engagement Services; (ii) Subscriptions and Perpetual Licenses; and (iii) Managed Service Hosting.

The Company recognizes revenue as required by the *Revenue Recognition* Topic of the Codification. Revenue is generally recognized when all of the following conditions are satisfied: (1) there is persuasive evidence of an arrangement; (2) delivery has occurred or the services have been provided to the customer; (3) the amount of fees to be paid by the customer is fixed or determinable; and (4) the collection of the fees is reasonably assured. Billings made or payments received in advance of providing services are deferred until the period these services are provided.

The Company maintains a reseller channel to supplement our direct sales force for our iAPPS platform. Resellers are generally located in territories where the Company does not have a direct sales force. Customers generally sign a license agreement directly with the Company. Revenue from perpetual licenses sold through resellers is recognized upon delivery to the end user as long as evidence of an arrangement exists, collectability is probable, and the fee is fixed and determinable. Revenue for subscription licenses is recognized monthly as the services are delivered.

Digital Engagement Services

Digital engagement services include professional services primarily related to the Company's web development solutions that address specific customer needs such as digital strategy, information architecture and usability engineering, .Net development, rich media development, back end integration, search engine optimization, quality assurance and project management.

Digital engagement services are contracted for on either a fixed price or time and materials basis. For its fixed price engagements, after assigning the relative selling price to the elements of the arrangement, the Company applies the proportional performance model (if not subject to contract accounting) to recognize revenue based on cost incurred in relation to total estimated cost at completion. The Company has determined that labor costs are the most appropriate measure to allocate revenue among reporting periods, as they are the primary input when providing application development services. Customers are invoiced monthly or upon the completion of milestones. For milestone based projects, since milestone pricing is based on expected hourly costs and the duration of such engagements is relatively short, this input approach principally mirrors an output approach under the proportional performance model for revenue recognition on such fixed priced engagements. For time and materials contracts, revenues are recognized as the services are provided.

Digital engagement services also include retained professional services contracted for on an "on call" basis or for a certain amount of hours each month. Such arrangements generally provide for a guaranteed availability of a number of professional services hours each month on a "use it or lose it" basis. For retained professional services sold on a stand-alone basis we recognize revenue as the services are delivered or over the term of the contractual retainer period. These arrangements do not require formal customer acceptance and do not grant any future right to labor hours contracted for but not used.

Managed Service Hosting

Managed service hosting includes hosting arrangements that provide for the use of certain hardware and infrastructure for those customers who do not wish to host the Company's applications independently. Hosting agreements are either annual or month-to-month arrangements that provide for termination for convenience by either party generally upon 30-days notice. Revenue is recognized monthly as the hosting services are delivered. Set up fees paid by customers in connection with managed hosting services are deferred and recognized ratably over the longer of the life of the hosting period or the expected lives of customer relationships. The Company will continue to evaluate the length of the amortization period of the set up fees as the Company gains more experience with customer contract renewals.

BRIDGELINE DIGITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

Subscriptions and Perpetual Licenses

The Company licenses its software on either a perpetual or subscription basis. Customers who license the software on a perpetual basis receive rights to use the software for an indefinite time period and an option to purchase post-customer support ("PCS"). For arrangements that consist of a perpetual license and PCS, as long as Vendor Specific Objective Evidence ("VSOE") exists for the PCS, then PCS revenue is recognized ratably on a straight-line basis over the period of performance and the perpetual license is recognized on a residual basis. Under the residual method, the fair value of the undelivered elements are deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and recognized as revenue, assuming all other revenue recognition criteria have been met.

Customers may also license the software on a subscription basis, which can be described as "Software as a Service" or "SaaS". SaaS is a model of software deployment where an application is hosted as a service provided to customers across the Internet. Subscription agreements include access to the Company's software application via an internet connection, the related hosting of the application, and PCS. Customers receive automatic updates and upgrades, and new releases of the products as soon as they become available. Customers cannot take possession of the software. Subscription agreements are either annual or month-to-month arrangements that provide for termination for convenience by either party upon 90 days notice. Revenue is recognized monthly as the services are delivered. Set up fees paid by customers in connection with subscription services are deferred and recognized ratably over the longer of the life of subscription period or the expected lives of customer relationships. The Company continues to evaluate the length of the amortization period of the set up fees as the Company gains more experience with customer contract renewals.

Multiple Element Arrangements

In accounting for multiple element arrangements, we follow either ASC Topic 605-985 *Revenue Recognition Software* or ASC Topic 605-25 *Revenue Recognition Multiple Element Arrangements*, as applicable.

In accordance with *Revenue Recognition: Multiple-Deliverable Revenue Arrangements*, each deliverable within a multiple-deliverable revenue arrangement is accounted for as a separate unit of accounting if both of the following criteria are met (1) the delivered item has value to the customer on a standalone basis and (2) for an arrangement that includes a right of return relative to the delivered item, delivery or performance of the delivered item is considered probable and within our control. If the deliverables do not meet the criteria for being a separate unit of accounting then they are combined with a deliverable that does meet that criterion. The accounting guidance also requires that arrangement consideration be allocated at the inception of an arrangement to all deliverables using the relative selling price method. The accounting guidance also establishes a selling price hierarchy for determining the selling price of a deliverable. We determine selling price using VSOE, if it exists; otherwise, we use Third-party Evidence ("TPE"). If neither VSOE nor TPE of selling price exists for a unit of accounting, we use Estimated Selling Price ("ESP").

VSOE is generally limited to the price at which we sell the element in a separate stand-alone transaction. TPE is determined based on the prices charged by The Company's competitors for a similar deliverable when sold separately. It is difficult for us to obtain sufficient information on competitor pricing, so we may not be able to substantiate TPE. If we cannot establish selling price based on VSOE or TPE then we will use ESP. ESP is derived by considering the selling price for similar services and our ongoing pricing strategies. The selling prices used in the Company's allocations of arrangement consideration are analyzed at minimum on an annual basis and more frequently if our business necessitates a more timely review. The Company has determined that the Company has VSOE on our SaaS offerings, certain application development services, managed hosting services, and PCS because we have evidence of these elements sold on a stand-alone basis.

BRIDGELINE DIGITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

When the Company licenses its software on a perpetual basis in a multiple element arrangement those arrangements typically includes PCS and application development services. In assessing the hierarchy of relative selling price for PCS, we have determined that VSOE is established for PCS. VSOE for PCS is based on the price of PCS when sold separately, which has been established via annual renewal rates. Similarly, when the Company licenses its software on a perpetual basis in a multiple element arrangement that also includes managed service hosting ("hosting"), we have determined that VSOE is established for hosting based on the price of the hosting when sold separately, which has been established based on renewal rates of the hosting contract. Revenue recognition for perpetual licenses sold with application development services are considered on a case by case basis. The Company has not established VSOE for perpetual licenses or fixed price development services and therefore in accordance with ASC Topic 605-985, when perpetual licenses are sold in multiple element arrangements including application development services where VSOE for the services has not been established, the license revenue is deferred and recognized using contract accounting. The Company has determined that services are not essential to the functionality of the software and it has the ability to make estimates necessary to apply proportional performance method. In those cases where perpetual licenses are sold in a multiple element arrangement that includes application development services where VSOE for the services has been established, the license revenue is recognized under the residual method and the application services are recognized upon delivery.

In determining VSOE for the digital engagement services element, the separability of the services from the software license and the value of the services when sold on a standalone basis are considered. The Company also considers the categorization of the services, the timing of when the services contract was signed in relation to the signing of the perpetual license contract and delivery of the software, and whether the services can be performed by others. The Company has concluded that its application development services are not required for the customer to use the product but, rather enhance the benefits that the software can bring to the customer. In addition, the services provided do not result in significant customization or modification of the software and are not essential to its functionality, and can also be performed by the customer or a third party. If an application development services arrangement does qualify for separate accounting, the Company recognizes the perpetual license on a residual basis. If an application development services arrangement does not qualify for separate accounting, the Company recognizes the perpetual license under the proportional performance model as described above.

When subscription arrangements are sold with application development services, the Company uses its judgment as to whether the application development services qualify as a separate unit of accounting. When subscription service arrangements involve multiple elements that qualify as separate units of accounting, the Company allocates arrangement consideration in multiple-deliverable arrangements at the inception of an arrangement to all deliverables based on the relative selling price model in accordance with the selling price hierarchy, which includes: (i) VSOE when available; (ii) TPE if VSOE is not available; and (iii) ESP if neither VSOE or TPE is available. For those subscription arrangements sold with multiple elements whereby the application development services do not qualify as a separate unit of accounting, the application services revenue is recognized ratably over the subscription period.

Subscriptions also include a PCS component, and the Company has determined that the two elements cannot be separated and must be recognized as one unit over the applicable service period. Set up fees paid by customers in connection with subscription arrangements are deferred and recognized ratably over the longer of the life of the hosting period or the expected lives of customer relationships, which generally range from two to three years. The Company continues to evaluate the length of the amortization period of the set up fees as we gain more experience with customer contract renewals and our newer product offerings.

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Customer Payment Terms

Payment terms with customers typically require payment 30 days from invoice date. Payment terms may vary by customer but generally do not exceed 45 days from invoice date. Invoicing for digital engagement services are either monthly or upon achievement of milestones and payment terms for such billings are within the standard terms described above. Invoicing for subscriptions and hosting are typically issued monthly and are generally due in the month of service.

The Company's digital engagement services agreements with customers do not provide for any refunds for services or products and therefore no specific reserve for such is maintained. In the infrequent instances where customers raise concerns over delivered services, the Company has endeavored to remedy the concern and all costs related to such matters have been insignificant in all periods presented. The Company’s subscription and hosting agreements provide for refunds when service is interrupted for an extended period of time and are reserved for in the month in which they occur if necessary.

Warranty

Certain arrangements include a warranty period, which is generally 30 days from the completion of work. In hosting arrangements, the Company provides warranties of up-time reliability. The Company continues to monitor the conditions that are subject to the warranties to identify if a warranty claim may arise. If it is determined that a warranty claim is probable, then any related cost to satisfy the warranty obligation is estimated and accrued. Warranty claims to date have been immaterial.

Reimbursable Expenses

In connection with certain arrangements, reimbursable expenses are incurred and billed to customers and such amounts are recognized as both revenue and cost of revenue.

Equipment and Improvements

The components of equipment are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets (three to five years). Leasehold improvements are amortized using the straight-line method over the lesser of the estimated useful life of the asset or the lease term. Repairs and maintenance costs are expensed as incurred.

Internal Use Software

Costs incurred in the preliminary stages of development are expensed as incurred. Once an application has reached the development stage, internal and external costs, if direct and incremental, are capitalized until the software is substantially complete and ready for its intended use. Capitalization ceases upon completion of all substantial testing. The Company also capitalizes costs related to specific upgrades and enhancements when it is probable that the expenditures will result in additional functionality. Capitalized costs are recorded as part of equipment and improvements. Training costs are expensed as incurred. Internal use software is amortized on a straight-line basis over its estimated useful life, generally three years.

Research and Development and Software Development Costs

Costs for research and development of a product to sell, lease or otherwise market are charged to operations as incurred until technological feasibility has been established. Once technological feasibility has been established, certain software development costs incurred during the application development stage are eligible for capitalization. Based on the Company’s product development process, technological feasibility is established upon completion of a working model.

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Software development costs that are capitalized are amortized to cost of sales over the estimated useful life of the software, typically three years. Capitalization ceases when a product is available for general release to customers. Capitalization costs are included in other assets in the consolidated financial statements. The Company capitalized $164 and $814 of costs in fiscal 2014 and fiscal 2013, respectively.

Intangible Assets

All intangible assets have finite lives and are stated at cost, net of amortization. Amortization is computed over the estimated useful life of the related assets on a straight-line method as follows:

Description	**Estimated Useful Life (in years)**
Developed and core technology	3
Non-compete agreements	3 - 6
Customer relationships	5 - 6
Trademarks and trade names	1 - 10

Business Combinations

We apply the appropriate guidance for business combination which requires goodwill to be recognized separately from the assets acquired and the liabilities assumed. Under this guidance, the assets acquired and the liabilities assumed are measured at fair value at the acquisition date. While the Company uses its best judgment to assign fair value, estimates are subject to refinement. The refinement period is one year from acquisition date. Adjustments are recorded to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. Any subsequent adjustments made after the one year refinement period are charged to the consolidated statement of operations.

Goodwill

Goodwill is tested for impairment annually during the fourth quarter of every year and more frequently if events and circumstances indicate that the asset might be impaired. In assessing goodwill for impairment, an entity has the option to assess qualitative factors to determine whether events or circumstances indicate that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount. We assess goodwill at the consolidated level as one reporting unit. If this is the case, then performing the quantitative two-step goodwill impairment test is unnecessary. An entity can choose not to perform a qualitative assessment for any or all of its reporting units, and proceed directly to the use of the two-step impairment test. In assessing qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we assess relevant events and circumstances that may impact the fair value and the carrying amount of a reporting unit. The identification of relevant events and circumstances and how these may impact a reporting unit's fair value or carrying amount involve significant judgments by management. These judgments include the consideration of macroeconomic conditions, industry and market considerations, cost factors, overall financial performance, events which are specific to the company, and trends in the market price of our common stock. Each factor is assessed to determine whether it impacts the impairment test positively or negatively, and the magnitude of any such impact.

For fiscal 2014 we performed the annual assessment of our goodwill during the fourth quarter of 2014, using the qualitative approach described above. Based on our qualitative assessment, we concluded that it was not more likely than not that the fair values of any of our reporting units were less than their carrying amounts, and therefore it was not necessary to perform the quantitative two-step impairment test. The key qualitative factors that led to our conclusion included the following: (i) Positive access to capital with two recent stock offerings totaling $5 million in capital; (ii) Positive market acceptance of our multi-unit products; and (iii) Fair market value of Company is in excess of book value.

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For fiscal 2013 we performed the annual assessment of our goodwill during the fourth quarter of 2013, using the qualitative approach described above. Based on our qualitative assessment, we concluded that it was not more likely than not that the fair values of any of our reporting units were less than their carrying amounts, and therefore it was not necessary to perform the quantitative two-step impairment test. The key qualitative factors that led to our conclusion included the following: (i) our stock price of $1.10 as of September 30, 2013 did not materially change from the stock price of $1.20 of September 30, 2012; (ii) the successful launch of iAPPSds in 2012 with our first iAPPSds customer, a franchisor with over 4,000 locations, and (iii) our strategic acquisition of ElementsLocal in fiscal 2013, has improved predictability of our forecasts by increasing contractually recurring revenue; and (iii) inputs from recent transactions within the technology sector, such as revenue multiples used to value transactions, have either remained steady since the fiscal 2011 assessment.

While there are inherent limitations in any valuation, the Company believes that placing a significant weighting of 75% on the Discounted Cash Flow Method, the Guideline Public Company Method, and the Guideline Transaction Method are more indicative of the fair value, or the price, that the Company would be sold at in an orderly transaction between market participants. The Company believes the most significant change in circumstances that could affect the key assumptions in our valuation are a significant reduction in the observed revenue multiples implied by future mergers and acquisitions and/or a significant deterioration of the Company's projected financial performance.

For all acquisitions completed before September 30, 2009, the Company records contingent consideration as additional purchase price and goodwill when earned. Such contingent consideration is unrelated to continuing employment with the Company and meets all other relevant criteria. For acquisitions completed after October 1, 2009, the Company records contingent consideration payments as additional purchase price and goodwill at the acquisition date. Any adjustments made within one year from the acquisition date are charged to goodwill. Any adjustment made after the one year refinement period will be charged to the consolidated statement of operations.

Valuation of Long-Lived Assets

The Company periodically reviews its long-lived assets, which consist primarily of property and equipment and intangible assets with finite lives, for impairment whenever events or changes in circumstances indicate the carrying amount of such assets may exceed their fair value. Recoverability of these assets is assessed using a number of factors including operating results, business plans, budgets, economic projections and undiscounted cash flows.

In addition, the Company's evaluation considers non-financial data such as market trends, product development cycles and changes in management's market emphasis. For the definite-lived intangible asset impairment review, the carrying value of the intangible assets is compared against the estimated undiscounted cash flows to be generated over the remaining life of the intangible assets. To the extent that the undiscounted future cashflows are less than the carrying value, the fair value of the asset is determined and impairment is recognized. If such fair value is less than the current carrying value, the asset is written down to the estimated fair value. There were no impairments in fiscal 2014 or 2013.

Deferred Revenue

Deferred revenue includes PCS and services billed in advance. PCS revenue, whether sold separately or as part of a multiple element arrangement, is deferred and recognized ratably over the term of the maintenance contract, generally 12 months. Payments made for PCS fees are generally made in advance and are nonrefundable. Revenue from consulting and training services is recognized as the related services are performed, using a proportional performance model.

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Fair Value of Financial Instruments

The Company's financial instruments consist principally of cash and cash equivalents, accounts receivable, accounts payable, and debt. Estimated fair values of amounts reported in the consolidated financial statements have been determined using available market information and valuation methodologies, as applicable. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Company believes the recorded values for accounts receivable and accounts payable approximate current fair values as of September 30, 2014 and September 30, 2013 because of their nature and durations. The carrying value of debt instruments also approximates fair value as of September 30, 2014 and September 30, 2013 based on acceptable valuation methodologies which use market data of similar size and situated debt issues.

Fair Value Measurements

For fair value measurements, the Company defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The use of market-based information over entity specific information is also prioritized and establishes a three-level hierarchy for fair value measurements based on the nature of inputs used in the valuation of an asset or liability as of the measurement date.

The hierarchy established under the Codification gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

Level 1 –Quoted prices in active markets for identical assets or liabilities;

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Foreign Currency

The Company determines the appropriate method of measuring assets and liabilities as to whether the method should be based on the functional currency of the entity in the environment it operates or the reporting currency of the Company, the U.S. dollar. The Company has determined that the functional currency of its Indian subsidiary is the Rupee. Assets and liabilities are translated into U.S. dollars at exchange rates in effect at the balance sheet date. Revenue and expense items are translated into U.S. dollars at average exchange rates for the period. The adjustments are recorded as a separate component of stockholders' equity and are included in accumulated other comprehensive income (loss). The Company's foreign currency translation net gains(losses) for fiscal 2014 and 2013 were $(171) and $14, respectively. Translation gains and losses related to monetary assets and liabilities denominated in a currency different from a subsidiary's functional currency are included in the consolidated statements of operations.

Segment Information

The Company operates internally as one reportable operating segment because all of the Company's locations have similar economic characteristics.

Stock-Based Compensation

The Company accounts for stock-based compensation in the consolidated statements of operations based on their fair values of the awards on the date of grant on a straight-line basis over their vesting term. Compensation expense is recognized only for share-based payments expected to vest. The Company estimates forfeitures at the date of grant based on the Company's historical experience and future expectations.

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Valuation of Stock Options and Warrants Issued to Non-Employees

The Company measures expense for non-employee stock-based compensation and the estimated fair value of options exchanged in business combinations and warrants issued for services using the fair value method for services received or the equity instruments issued, whichever is more readily measured. The Company estimated the fair value of stock options issued to non-employees using the Black-Scholes Merton option valuation model.

The Company estimated the fair value of common stock warrants issued to non-employees using the binomial options pricing model. The Company evaluates common stock warrants as they are issued to determine whether they should be classified as an equity instrument or a liability. Those warrants that are classified as a liability are carried at fair value at each reporting date, with changes in their fair value recorded in other income (expense) in the consolidated statements of operation.

Advertising Costs

Advertising costs are expensed when incurred. Such costs were $768 and $808 for fiscal 2014 and 2013, respectively.

Employee Benefits

The Company sponsors a contributory 401(k) plan allowing all full-time employees who meet prescribed service requirements to participate. The Company is not required to make matching contributions, although the plan provides for discretionary contributions by the Company. The Company made no contributions in either fiscal 2014 or fiscal 2013.

Income Taxes

The Company recognizes deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the Company's financial statements and tax returns. Deferred income taxes are recognized based on temporary differences between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the temporary differences are expected to reverse. Valuation allowances are provided if based upon the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

The Company provides for reserves for potential payments of taxes to various tax authorities related to uncertain tax positions. Reserves are based on a determination of whether and how much of a tax benefit taken by the Company in its tax filings or positions is "more likely than not" to be realized following resolution of any uncertainty related to the tax benefit, assuming that the matter in question will be raised by the tax authorities. Interest and penalties associated with uncertain tax positions are included in the provision for income taxes.

The Company does not provide for U.S. income taxes on the undistributed earnings of its Indian subsidiary, which the Company considers to be permanent investments.

Comprehensive Loss

The Company's comprehensive loss is comprised of net loss and foreign currency translation adjustments.

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Net Loss Per Share

Basic net loss per share is computed by dividing net loss available to common shareholders by the weighted average number of common shares outstanding. Diluted net income per share is computed using the weighted average number of common shares outstanding during the period plus the dilutive effect of outstanding stock options and warrants using the "treasury stock" method. The computation of diluted earnings per share does not include the effect of outstanding stock options and warrants that are anti-dilutive.

Recent Accounting Pronouncements

In June 2014, the Financial Accounting Standards Board ("FASB") issued a standards update on accounting for share-based payments when the terms of the award provide that a performance target could be achieved after a requisite service period. The standard is effective beginning January 1, 2016, with early adoption permitted. Management does not expect it to have a material impact on our consolidated financial position, results of operations or cash flows.

In May 2014, the FASB issued a standard on revenue recognition providing a single, comprehensive revenue recognition model for all contracts with customers. The revenue standard is based on the principle that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard is effective beginning January 1, 2017, with no early adoption permitted. The amendments may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of initial application. Management is currently evaluating the adoption method options and the impact of this new guidance on our condensed consolidated financial statements.

In April 2014, the FASB issued new accounting guidance on reporting discontinued operations and disclosures of disposals of components of an entity which clarifies the scope of what should be reported as discontinued operations and expands required disclosures. This new guidance is effective beginning October 1, 2015, with early adoption permitted. The impact of this guidance will be dependent on the nature and significance of any transactions within the scope of this new guidance.

In July 2013, the FASB issued new guidance on the presentation of unrecognized tax benefits. This guidance requires an unrecognized tax benefit related to a net operating loss carryforward, a similar tax loss or a tax credit carryforward to be presented as a reduction to a deferred tax asset, unless the tax benefit is not available at the reporting date to settle any additional income taxes under the tax law of the applicable tax jurisdiction. The guidance is effective for the fiscal years and interim periods beginning after December 15, 2013 with early adoption permitted. Management is in the process of evaluating the effects of this guidance but does not believe it will have a significant impact on our condensed consolidated financial statements.

In March 2013, the FASB issued ASU No. 2013-05, "Foreign Currency Matters (Topic 830): Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity ." This ASU addresses the accounting for the cumulative translation adjustment when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. The guidance outlines the events when cumulative translation adjustments should be released into net income and is intended by FASB to eliminate some disparity in current accounting practice. This ASU is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013 (fiscal 2015). The amendments should be applied prospectively to derecognition events occurring after the effective date. Prior periods should not be adjusted. Early adoption is permitted. If an entity elects to early adopt the amendments, it should apply them as of the beginning of the entity's fiscal year of adoption. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position and results of operations.

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3. Accounts Receivable and Unbilled Receivables

Accounts receivable and unbilled receivables consists of the following:

	September 30,	
	2014	**2013**
Accounts receivable	$3,303	$3,188
Unbilled receivables	229	111
Subtotal	3,532	3,299
Allowance for doubtful accounts	(190)	(105)
Accounts receivable and unbilled receivables, net	$3,342	$3,194

4. Equipment and Improvements

Equipment and improvements consists of the following:

	September 30,	
	2014	**2013**
Furniture and fixtures	$1,480	$1,521
Purchased software	1,037	973
Computers and equipment	4,307	4,143
Leasehold improvements	1,756	1,828
Total cost	8,580	8,465
Less accumulated depreciation	(6,405)	(5,400)
Equipment and improvements, net	$2,175	$3,065

Depreciation and amortization on the above assets was $1.3 million and $1.2 million in fiscal 2014 and 2013, respectively.

5. Acquisitions

On August 1, 2013, the Company completed the acquisition of Transformational Technologies, Inc ("ElementsLocal"), a California based developer of an online SaaS platform for the franchise marketplace. The Company acquired all of the outstanding capital stock of ElementsLocal for consideration consisting of (i) $463 in cash; (ii) $604 in shares of Bridgeline Digital common stock (valued at $1.15 per share); (iii) assumption of $188 of indebtedness; and (iv) contingent consideration of up to $904 in cash and $396 in shares of Bridgeline Digital common stock. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving a certain quarterly revenue target during the period. The contingent common stock payable each earnout period is determined by dividing $33 by the greater of: (i) the average closing price for Bridgline Digital common stock for the 30 day trading period preceding the end of the earnout period; or (ii) $1.17. To the extent that a quarterly revenue target is not met in a particular quarter, the earn-out period will be extended for up to four additional quarters. The Company is required to assess the probability of the acquired business achieving the contingent cash and stock payments which requires management to make estimates and judgments based on forecasts of future performance. ElementsLocal's operating results are reflected in the Company's condensed consolidated financial statements as of the acquisition date. As of September 30, 2014, the stockholders of ElementsLocal achieved each scheduled earnout for the periods presented.

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The estimated fair value of net assets acquired from the acquisition of ElementsLocal are summarized as follows:

Net assets acquired:	**Amount**
Cash	$ 100
Accounts Receivable, net	139
Other Assets	-
Fixed Assets	-
Intangible Assets	1,310
Goodwill	1,186
Total Assets	2,735
Current Liabilities	368
Liabilities, net of current	-
Total liabilities assumed	368
Net assets acquired:	$ 2,367
Purchase Price:	
Cash Paid	$ 463
Common stock issued	604
Contingent earnouts - payable in cash	904
Contingent earnouts - payable in common stock	396
	$ 2,367

As part of the ElementsLocal acquisition $1.3 million was allocated to intangible assets; $1.1 million of which was allocated to customer relationships, $220 was allocated to a non-compete agreement, and $20 was allocated to trademarks with an average useful life of seven, five and two years, respectively. The goodwill recorded as a result of the ElementsLocal acquisition is nondeductible for tax purposes.

The following unaudited pro forma financial information reflects the combined results of operations for Bridgeline for the fiscal 2013. This information does not necessarily reflect the results of operations that would have occurred had the acquisitions taken place at the beginning of the period, and is not necessarily indicative of the results which may be obtained in the future:

Total revenue	$26,175
Net loss	(3,566)

Net loss per share	
Basic and diluted	$(0.22)
Number of weighted average shares	
Basic and diluted	16,067,455

6. Fair Value Measurement and Fair Value of Financial Instruments

The Company's other financial instruments consist principally of accounts receivable, accounts payable, and debt. The Company believes the recorded values for accounts receivable and accounts payable approximate current fair values as of September 30, 2014 and 2013 because of their nature and durations. The carrying value of debt instruments also approximates fair value as of September 30, 2014 and 2013 based on acceptable valuation methodologies which use market data of similar size and situated debt issues.

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Assets and liabilities of the Company measured at fair value on a recurring basis as of September 30, 2014 and 2013 are as follows:

	September 30, 2014			
	Level 1	**Level 2**	**Level 3**	**Total**
Liabilities:				
Contingent acquisition consideration	$ -	$ -	$ 868	$ 868
Warrant liability	-	-	39	39
Total Liabilities	$ -	$ -	$ 907	$ 907

	September 30, 2013			
	Level 1	**Level 2**	**Level 3**	**Total**
Liabilities:				
Contingent acquisition consideration	$ -	$ -	$ 1,511	$ 1,511
Warrant liability	-	-	-	-
Total Liabilities	$ -	$ -	$ 1,511	$ 1,511

The Company determines the fair value of acquisition-related contingent consideration based on assessment of the probability that the Company would be required to make such future payments. Changes to the fair value of contingent consideration are recorded in general and administrative expenses. The following table provides a rollforward of the fair value, as determined by Level 3 inputs, of the contingent consideration.

The following table summarizes the changes in contingent consideration for the fiscal year ended September 30, 2014 and 2013:

	Year Ended September 30,	
	2014	**2013**

Beginning balance	$1,511	$1,365
Additions	-	933
Payments	(643)	(531)
Other adjustments	-	(256)
Ending balance	$868	$1,511

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The following table summarizes the changes in warrant liability for the fiscal year ended September 30, 2014 and 2013:

	Year Ended September 30, 2014	**2013**
Beginning balance	$ -	$ -
Warrant liability	72	-
Fair market value adjustment	(33)	-
Ending balance	$ 39	$ -

7. Intangible Assets

Changes in the carrying amount of intangible assets are as follows:

	September 30, 2014	**2013**
Domain and trade names	$10	$34
Customer related	1,284	1,182
Non-compete agreements	288	301
Balance at end of period	$1,582	$1,517

Total amortization expense related to intangible assets for the years ended September 30, 2014 and 2013 is reflected in the Company's Consolidated Statements of Operations in depreciation and amortization. The estimated amortization expense for fiscal years 2015, 2016, 2017, and 2018 is: $559, $428, $369, $215, respectively.

8. Goodwill

Changes in the carrying amount of goodwill are as follows:

	September 30, 2014	2013
Balance at beginning of period	$23,777	$21,545
Acquisitions	-	1,897
Contingent acquisition payments	-	83
Purchase price allocation adjustments	(636)	252
Balance at end of period	$23,141	$23,777

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9. Accrued Liabilities

Accrued liabilities consist of the following:

	September 30,	
	2014	**2013**
Compensation and benefits	$312	$418
Professional fees	164	252
Deferred rent (1)	140	117
Reseller commissions	62	15
Accrued taxes	41	6
Subcontractors	72	25
Other	166	260
Total	$957	$1,093

(1) The deferred rent liability is being amortized as a reduction of rent expense over the lives of the leases. As of September 30, 2014, $140 was reflected in Accrued Liabilities and $740 is reflected in Other Long Term Liabilities on the Consolidated Balance Sheet as deferred rent liabilities.

10. Debt

Debt consists of the following:

	September 30,	
	2014	**2013**
Line of credit borrowings	$2,938	$3,504
Bank term loan	1,000	272
Subordinated convertible debt	3,000	2,000

Subordinated promissory note	21	114
Subtotal debt	6,959	5,890
Other (debt warrants)	(39)	-
Total debt	$6,920	$5,890
Less current portion	$985	$1,165
Long term debt, net of current portion	$5,935	$4,725

Line of Credit and Bank Term Loan

In December 2013, the Company entered into a Loan and Security Agreement with BridgeBank (the "BridgeBank Loan Agreement"). The BridgeBank Loan Agreement replaced the Company's prior credit facility with Silicon Valley Bank ("SVB"), which expired on December 31, 2013 (See below). The Loan Agreement has a 27 month term which expires on March 31, 2016. The Loan Agreement provides for up to $5 million of revolving credit advances which may be used for acquisitions and working capital purposes. Borrowings are limited to the lesser of (i) $5 million and (ii) 80% of eligible receivables as defined. The Company can borrow up to $1.0 million in out of formula borrowings for specified periods of time. Borrowings bear interest at BridgeBank's prime plus 1.00%. The Company pays an annual commitment fee of 0.25%. Borrowings are secured by all of the Company's assets and all of the Company's intellectual property. The Company is also required to comply with certain financial and reporting covenants including an Asset Coverage Ratio. As of September 30, 2014, the Company had an outstanding balance under the BridgeBank Loan Agreement of $2.9 million. The Company was in compliance with all reporting covenants for the period ended September 30, 2014, except for certain financial covenants. The Company obtained a waiver for the financial covenants that it was not in compliance with and further modified the BridgeBank Loan Agreement to amend the covenants prospectively. (See Subsequent Events)

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The Company had an Amended and Restated Loan and Security Agreement with SVB (the “Loan Agreement”). The Loan Agreement had a two year term which expired on March 31, 2012. The Loan Agreement provided for up to \$5.0 million of revolving credit advances, of which \$3.0 million may be used for acquisitions and up to \$5.0 million may be used for working capital purposes. Borrowings were limited to the lesser of (i) \$5.0 million and (ii) 80% of eligible receivables as defined. In the event that the borrowing base formula resulted in less than \$5.0 million in available borrowing, the Company could have borrowed up to \$2.0 million in out of formula borrowings (provided such amount does not exceed \$5.0 million) for specified periods of time. Borrowings bore interest at SVB’s prime plus 1.00% or 1.25%, depending on the level of the adjusted EBITDA, as defined. The Company paid an annual commitment fee of 0.50% and an unused fee of 0.25%. Borrowings were secured by all of the Company’s assets and all of the Company’s intellectual property. The Company was also required to comply with certain financial and performance covenants.

In addition, the Company had a \$2 million term loan and interest on the term loan will be at SVB’s prime rate plus 1.75%. Interest on the term loan was paid until April 1, 2012 and on and after April 2, 2012, principal and interest on the term loan was being paid over 36 months ending on April 1, 2015. In May 2012, we amended our loan agreement (the “2012 Amendment”) with SVB, extending the maturity date of the line of credit for one year to March 31, 2014. The 2012 Amendment also revised a financial covenant, increasing our minimum liquidity requirement. Minimum liquidity is defined as funds held with SVB plus borrowing availability on our line of credit.

In February 2013, the Company amended its loan agreement (the “February 2013 Amendment”) with SVB, extending the maturity date of the line of credit for one year to March 31, 2015. The 2013 Amendment also revised certain financial covenants. The Company would not have been in compliance with one of its covenants for the three months ended December 31, 2012 if the amendment was not completed. In July 2013, the Company amended its loan arrangement (the “July 2013 Amendment”) with SVB. The July 2013 Amendment increased the borrowing availability on accounts receivable, revised certain financial covenants, and increased the interest rate on the line of credit from prime plus 1.25% to prime plus 2.25% and increased the interest rate on the term loan from prime plus 1.75% to prime plus 2.75%. In addition, the repayment schedule for the term loan was accelerated to end in April 2014. There was \$611 remaining on the term loan as of June 30, 2013. The July 2013 Amendment also included a waiver by SVB of certain financial covenant defaults. The Company would not have been in compliance with certain of its financial covenants as of June 30, 2013 if the July 2013 Amendment had not been completed and the waiver had not been granted. In November 2013, the Company amended its loan agreement (“the November 2013 Amendment”) with SVB. The November 2013 Amendment accelerated the maturity date of the line of credit to December 31, 2013 at which time this line was replaced with the BridgeBank Loan Agreement and the term loan was paid in full.

At September 30, 2013, the Company had an outstanding balance under the term loan with SVB of \$272, which was repaid in December 2013. At September 30, 2014, the Company had an outstanding short term loan with BridgeBank of $1.0 million which was repaid in October 2014.

Subordinated Convertible Debt

On September 30, 2013, Bridgeline Digital entered into a Note Purchase Agreement (the "Purchase Agreement") with accredited investors pursuant to which Bridgeline Digital sold an aggregate of $2.0 million of 10% secured subordinated convertible notes (the "Notes"). The gross proceeds to Bridgeline Digital at the closing of this private placement were $2.0 million. The Notes accrue interest at a rate of ten percent (10%) per annum and mature on September 30, 2016. Interest on the Notes is payable quarterly in cash. The Notes are convertible at the election of the holder into shares of common stock of Bridgeline Digital at a conversion price equal to $1.30 per share at any time prior to the maturity date, provided that no holder may convert the Notes if such conversion would result in the holder beneficially owning more than 4.99% of the number of shares of Bridgeline Digital common stock outstanding at the time of conversion.

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On November 6, 2013, Bridgeline Digital entered into an amendment (the "Amendment") to the Purchase Agreement by and among Bridgeline Digital and the accredited investors’ party thereto. The Amendment increased the aggregate amount of 10% secured subordinated convertible notes (the "New Notes") able to be sold by Bridgeline Digital to $3.0 million. On November 6, 2013, Bridgeline Digital sold an additional $1.0 million of New Notes (the "Second Closing"). The gross proceeds to Bridgeline Digital at the Second Closing of this private placement were $1.0 million. The Notes accrue interest at a rate of ten percent (10%) per annum and mature on November 6, 2016. Interest on the Notes is payable quarterly in cash. The Notes are convertible at the election of the holder into shares of common stock of Bridgeline Digital at a conversion price equal to $1.30 per share at any time prior to the maturity date, provided that no holder may convert the Notes if such conversion would result in the holder beneficially owning more than 4.99% of the number of shares of Bridgeline Digital common stock outstanding at the time of conversion.

The Notes are secured by all of Bridgeline Digital's assets. The security interest granted to the holders of the Notes is subordinate to the security interest held by Bridgeline Digital's senior lender, BridgeBank. Bridgeline Digital may prepay any portion of the principal amount of the outstanding Notes at any time, provided that if Bridgeline Digital prepays any principal on or before September 30, 2014, Bridgeline Digital will pay a penalty equal to 10% of the principal amount being prepaid. Under certain circumstances Bridgeline Digital has the right to force conversion of the Notes into shares of Bridgeline Digital common stock in the event the Bridgeline Digital common stock trades in excess of $2.60 per share for 20 trading days out of any 30 trading day period.

The Notes contain customary events of default. Upon the occurrence of any event of default the interest rate under the Notes will increase. In addition, upon the occurrence of a payment default under the Notes, Bridgeline Digital must pay a premium equal to 20% of the outstanding principal amount of the Notes. In the event of a change in control of Bridgeline Digital while the Notes are outstanding, Bridgeline Digital will provide the holders of the Notes with the opportunity to convert the Notes immediately prior to the change in control. In the event the holders of the Notes do not elect to convert the Notes, Bridgeline Digital may prepay all outstanding principal and accrued interest under the Notes.

The placement agent for both transactions was Taglich Brothers, Inc. As compensation for the initial transaction on September 30, 2013, Bridgeline Digital paid a fee of $160 and issued to Taglich Brothers, Inc., or its designees, five-year warrants to purchase an aggregate of 153,846 shares of common stock at an exercise price equal to $1.30 per share. The warrants are first exercisable on March 30, 2014, and provide the holders piggyback registration rights with respect to the shares of common stock underlying the warrants and contain a cashless exercise provision. As compensation for the Second Closing, Bridgeline Digital paid Taglich Brothers, Inc. a fee of $80 and issued to Taglich Brothers, Inc., or its designees, five-year warrants to purchase an aggregate of 76,923 shares of common stock at an exercise price equal to $1.30 per share. The warrants are first exercisable on May 6, 2014, provide the holders piggyback registration rights with respect to the shares of common stock underlying the warrants and contain a cashless exercise provision. Fair market value of the warrants are $49 and is included in current liabilities and non-current debt with the offsetting amount recorded to additional paid in capital in the Condensed Consolidated Balance Sheet. The fair market value of the warrants will be amortized on a straight-line basis over the estimated life of two years.

The shares of common stock issuable upon conversion of the Notes and upon exercise of the warrants are restricted securities and may be sold only pursuant to Rule 144 or in another transaction exempt from the registration requirements under the Securities Act of 1933. Pursuant to the terms of the Purchase Agreement, Bridgeline Digital has agreed to provide piggyback registration rights with respect to the shares of common stock issuable upon conversion of the Notes in the event Bridgeline Digital files a registration statement, with certain limited exceptions.

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Subordinated Promissory Notes

In May 2010, in connection with the acquisition of TMX, the Company issued a $500 subordinated promissory note ("the Note") payable to TMX. The Note is subordinated to the Company's primary lender and is payable in twelve quarterly installments of $42, plus interest at 1%, with the first payment due on January 15, 2011. The Note may be paid in whole or in part at any time without discount, premium, or penalty.

In May 2012, the Company assumed two Promissory Notes in connection with the acquisition of MarketNet, Inc. The first Promissory Note in the amount of $63 is payable in eight equal installments of $8, including interest accrued at 5%, and matured in May 2014. This note was paid in full at September 30, 2014. The first installment was paid in July 2012. The second Promissory Note in the amount of $80 is payable in twelve equal installments of $7, including interest accrued at 5%, and matures in May 2015. The first installment was paid in July 2012.

As of September 30, 2014, the Company had the following minimum debt obligation payments remaining:

Year Ending September 30,	Amount
2015	$ 1,021
2016	4,938
2017	1,000
Total	$ 6,959
Less interest	$ (69)
Total debt obligations	$ 6,890

11. Commitments and Contingencies

Operating Lease Commitments

We lease our facilities in the United States and India. Future minimum rental commitments under non-cancelable operating leases with initial or remaining terms in excess of one year at September 30, 2014 were as follows:

Year Ending September 30,	Amount
2015	$ 1,342
2016	1,265
2017	999
2018	905
2019 and thereafter	504
Total	$ 5,015

Rent expense for fiscal 2014 and 2013 was $1,500 for both periods, inclusive of sublease income of $24 and $24 for fiscal 2014 and 2013, respectively.

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Capital Lease Obligations

	September 30,	
	2014	**2013**
Capital lease obligations	$611	$941
Less: Current portion	(364)	(397)
Capital lease obligations	$247	$544

As of September 30, 2014, the Company's future minimum lease payments due under capitalized lease obligations due in fiscal 2015 and 2016 consist of $364 and $247, respectively.

Other Commitments, Guarantees, and Indemnification Obligations

The Company frequently warrants that the technology solutions it develops for its clients will operate in accordance with the project specifications without defects for a specified warranty period, subject to certain limitations that the Company believes are standard in the industry. In the event that defects are discovered during the warranty period, and none of the limitations apply, the Company is obligated to remedy the defects until the solution that the Company provided operates within the project specifications. The Company is not typically obligated by contract to provide its clients with any refunds of the fees they have paid, although a small number of its contracts provide for the payment of liquidated damages upon default. The Company has purchased insurance policies covering professional errors and omissions, property damage and general liability that reduce its monetary exposure for warranty-related claims and enable it to recover a portion of any future amounts paid.

The Company's contracts typically provide for testing and client acceptance procedures that are designed to mitigate the likelihood of warranty-related claims, although there can be no assurance that such procedures will be effective for each project. The Company has not paid any material amounts related to warranties for its solutions. The Company sometimes commits unanticipated levels of effort to projects to remedy defects covered by its warranties. The Company's estimate of its exposure to warranties on contracts is immaterial as of September 30, 2014.

The Company's agreements with customers generally require the Company to indemnify the customer against claims in which the Company's products infringe third-party patents, copyrights, or trademarks and indemnify against product liability matters. As of September 30, 2014 and 2013, respectively, the Company has not experienced any losses related to the indemnification obligations and no significant claims with respect thereto were outstanding. The Company does not expect significant claims related to the indemnification obligations and, consequently, concluded that the fair value of these obligations is negligible, and no related reserves were established.

Litigation

The Company is subject to ordinary routine litigation and claims incidental to its business. As of September 30, 2014, Bridgeline was not engaged with any material legal proceedings.

12. Shareholder's Equity

Common Stock

In March 2014, the Company sold 3,200,000 shares of common stock at $0.95 per share for gross proceeds of $3 million in a private placement. Net proceeds to the Company after offering expenses were approximately $2.7 million. In addition, the Company issued the placement agent five year warrants to purchase an aggregate of 320,000 shares of Bridgeline's common stock at a price equal to $1.05 per share. There are no plans to register the common stock issued in this offering, however in the event the Company does register other Common stock, the Company agreed to provide piggyback registration rights with respect to the shares of common stock sold in the offering and underlying the warrants.

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In January 2014, the Company issued 56,897 shares of common stock at $1.16 per share to four members of its Board of Directors in lieu of cash payments for their services as board members. The shares vest in equal installments on a monthly basis through the end of the service period of September 30, 2014. The aggregate fair value of the shares is $66 and will be expensed over the service period. A total of $19 was recorded as expense in the three months ended June 30, 2014.

On June 19, 2013, the Company sold 2,300,000 shares of common stock at $1.00 per share for gross proceeds of $2.3 million in a private placement. Net proceeds to the Company after offering expenses were approximately $2.1 million. In addition, the Company issued the investors and placement agent and its affiliates five year warrants to purchase an aggregate of 460,000 and 230,000 shares, respectively, of Bridgeline's common stock at a price equal to $1.25 per share. There are no plans to register the common stock issued in this offering, however in the event the Company does register other Common stock, the Company agreed to provide piggyback registration rights with respect to the shares of common stock sold in the offering and underlying the warrants.

Contingent Consideration

In connection with the acquisition of ElementsLocal on August 1, 2013, the Company issued 526,438 shares to the sellers of ElementsLocal. In addition, contingent consideration not to exceed 338,461 shares of Bridgeline Digital common stock is contingently issuable to the sellers of ElementsLocal. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain revenue targets. As of September 30, 2014, the stockholders of ElementsLocal earned 112,820 shares of common stock.

In connection with the acquisition of MarketNet on May 31, 2012, contingent consideration of 204,331 shares of Bridgeline Digital common stock is contingently issuable to the sole stockholder of MarketNet. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain operating and revenue targets. The common stock has been issued and is being held in escrow pending satisfaction of the applicable earnout targets. As of September 30, 2014, the sole stockholder of MarketNet earned 136,224 shares of common stock. In addition, MarketNet is also eligible to earn additional equity consideration of 200,000 shares of Bridgeline Digital common stock if a certain annual revenue threshold is met in any fiscal year during the next three years.

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In connection with the acquisition of Magnetic Corporation on October 3, 2011, contingent consideration of 166,666 shares of Bridgeline Digital common stock is contingently issuable to the sole stockholder of Magnetic. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain operating and revenue targets. The common stock has been issued and is being held in escrow pending satisfaction of the applicable earnout targets. As of September 30, 2014, the sole stockholder of Magnetic earned the full value or 166,666 shares of common stock.

Amended and Restated Stock Incentive Plan

The Company has granted common stock, common stock warrants, and common stock option awards (the “Equity Awards”) to employees, consultants, advisors and debt holders of the Company and to former owners and employees of acquired companies that have become employees of the Company. At September 30, 2014, the Company maintained one stock option plan and one employee stock purchase plan.

In order to increase employee retention and morale, in October 2011, the Company offered its employees the opportunity to have certain outstanding options modified by (i) reducing the grant exercise price to $0.67, the fair market value of the common stock as of the modification date and (ii) starting a new three year vesting schedule. The aggregate fair value of the modified options of approximately $90 was calculated using the difference in value between the original terms and the new terms as of the modification date. The incremental cost of the modified option over the original option will be recognized as additional compensation expense over the new three year vesting period beginning on the date of modification. This opportunity was generally limited to options issued subsequent to the October 2008 repricing described in Note 11 to the Company’s Annual Report on Form 10-K for fiscal 2011. Options to purchase a total of 697,667 shares of common stock were exchanged for new grants in the October 28, 2011 repricing.

Effective August 2014, the Company’s Amended and Restated Stock Incentive Plan (the “Plan”) provides for the issuance of up 4,500,000 million shares of common stock. The Plan authorizes the award of incentive stock options, non-statutory stock options, restricted stock, unrestricted stock, performance shares, stock appreciation rights and any combination thereof to employees, officers, directors, consultants, independent contractors and advisors of the Company.   Options granted under the Plan may be granted with contractual lives of up to ten years. There were 3,535,640 options outstanding reserved under the Plan as of September 30, 2014 and 964,360 shares available for future issuance.

Employee Stock Purchase Plan

On April 12, 2012, the Company's stockholders approved and adopted the Bridgeline Digital, Inc. 2012 Employee Stock Purchase Plan (the "ESPP"). Under the terms of the ESPP, the Company will grant eligible employees the right to purchase shares of Bridgeline common stock through payroll deductions at a price equal to 85% of the fair market value of Bridgeline common stock on the purchase termination date of defined offering or purchase periods. Each offering period is six months in duration. The ESPP permits the Company to offer up to 300,000 shares of common stock. The maximum number of shares of common stock that may be purchased by all participants in any purchase period may not exceed 150,000 shares. As of September 30, 2014, 82,660 shares were issued under the ESPP plan.

Common Stock Warrants

In March 2014, the Company issued five year warrants to the investors and placement agent in the Company's private placement. The warrants are exercisable to purchase 320,000 shares of the Company's common stock at a price equal to $1.05 per share.

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In November 2013, the Company issued five year warrants to the placement agent in the Company's placement of subordinated convertible debt. The warrants are exercisable to purchase 76,923 shares of the Company's common stock at a price equal to $1.30 per share. The warrants are first exercisable on May 6, 2014, provide the holders piggyback registration rights with respect to the shares of common stock underlying the warrants and contain a cashless exercise provision.

In September 2013, the Company issued five year warrants to the placement agent in the Company's placement of subordinated convertible debt. The warrants are exercisable to purchase 153,846 of the Company's common stock at a price equal to $1.30 per share. The warrants are first exercisable on March 30, 2014, provide the holders piggyback registration rights with respect to the shares of common stock underlying the warrants and contain a cashless exercise provision.

In June 2013, the Company issued five year warrants to the investors and placement agent in the Company's private placement. The warrants are exercisable to purchase 460,000 and 230,000 shares, respectively, of the Company's common stock at a price equal to $1.25 per share.

In May 2012, the Company issued five year warrants to the placement agent in the Company's private placement. The warrants are exercisable to purchase 217,931 shares of the Company's common stock at a price equal to $1.40 per share.

In October, 2010, the Company issued 50,000 common stock warrants to purchase shares of the Company's common stock to a non-employee consultant as compensation for services rendered. The warrants vested over a one year period and expire on October 15, 2015. Of the warrants issued, 25,000 are exercisable at an exercise price of $1.00 per share and 25,000 are exercisable at an exercise price of $2.00 per share.

As of September 30, 2014: (i) placement agent warrants to purchase 217,931, 230,000, 230,769, and 320,000 shares at an exercise price of $1.40, $1.25, $1.30 and $1.05, respectively are outstanding; (ii) investor warrants to purchase 460,000 shares at an exercise price of $1.25, and (iii) warrants issued to a non-employee consultant to purchase 25,000 shares at an exercise price of $1.00 and 25,000 shares at an exercise price of $2.00 are outstanding.

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Stock Option and Warrant Activity and Outstanding Shares

A summary of combined option and warrant activity follows:

	Stock Options		**Stock Warrants**	
	Options	**Weighted Average Exercise Price**	**Warrants**	**Weighted Average Exercise Price**
Outstanding, September 30, 2012	2,989,620	$ 1.00	331,931	$ 1.42
Granted	441,500	$ 1.63	843,846	$ 1.26
Exercised	(199,573)	$ 0.81	(22,599)	$ 1.45
Forfeited or expired	(358,703)	$ 1.15	(41,401)	$ 1.45
Outstanding, September 30, 2013	2,872,844	$ 0.86	1,111,777	$ 1.30
Granted	1,197,500	$ 1.10	396,923	$ 1.10
Exercised	(261,086)	$ 0.43	-	-
Forfeited or expired	(273,618)	$ 1.36	-	-
Outstanding, September 30, 2014	3,535,640	$ 0.98	1,508,700	$ 1.25

There were 261,086 options exercised during the year ended September 30, 2014, with an intrinsic value of $44. There were 199,573 options exercised during the year ended September 30, 2013, with an intrinsic value of $97. There were 1,748,387 options vested and exercisable as of September 30, 2014 with an intrinsic value of $10. The intrinsic value was calculated based on the gross difference between the Company’s closing stock price on the last day of trading of fiscal 2014 and the exercise prices for all in-the money options vested and exercisable, excluding tax effects.

A summary of the status of nonvested shares is as follows:

	Weighted Average Grant-Date

	Shares	Fair Value
Nonvested at September 30, 2013	1,469,145	$ 0.56
Granted	1,197,500	0.74
Vested	(633,387)	0.46
Forfeited	(246,005)	0.88
Nonvested at September 30, 2014	1,787,253	$ 0.67

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Price ranges of outstanding and exercisable options as of September 30, 2014 are summarized below:

Outstanding Options						**Exercisable Options**	
Exercise Price			**Number of Options**	**Weighted Average Remaining Contractual Life (Years)**	**Weighted Average Exercise Price**	**Number of Options Exercisable**	**Weighted Average Exercise Price**
$0.01	to	$0.75	1,110,626	7.10	$ 0.65	708,890	$ 0.65
$0.76	to	$1.00	807,514	5.22	0.89	664,180	0.89
$1.01	to	$1.64	1,617,500	8.50	1.24	375,317	1.32
			3,535,640	7.31	$ 0.98	1,748,387	$ 0.89

Compensation Expense

The Company estimates the fair value of stock options using the Black-Scholes-Merton option valuation model (the "Model"). The assumptions used to calculate compensation expense is as follows:

	Year Ended September 30,	
	2014	**2013**
Expected option life in years	6.0	6.0
Expected volatility	78.70%	80.60%
Expected dividend rate	0.00%	0.00%
Risk free interest rate	1.55%	1.14%
Option exercise prices	$0.92 to $1.29	$1.09 to $2.33
Weighted average fair value of options granted during the year	$0.74	$0.35

Compensation expense is generally recognized on a graded accelerated basis over the vesting period of grants. During the years ended September 30, 2014 and 2013, the Company recognized $449 and $438, respectively, as compensation expense related to share based payments. As of September 30, 2014, the Company had approximately $424 of unrecognized compensation costs related to unvested options which the Company expects to recognize through fiscal 2017.

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13. Income Taxes

The components of the Company's tax provision as of September 30, 2014 and 2013 is as follows:

	Year Ended September 30,	
	2014	**2013**
Current:		
Federal	$-	$-
State	24	23
Foreign	-	46
Total current	24	69
Deferred:		
Federal	180	89
State	39	13
Total deferred	219	102
Grand Total	$243	$171

The Company’s income tax provision was computed using the federal statutory rate and average state statutory rates, net of related federal benefit. The provision differs from the amount computed by applying the statutory federal income tax rate to pretax income., as follows:

	Year Ended September 30,	
	2014	**2013**
Income tax benefit at the federal statutory rate of 34%	$(1,963)	$(1,205)
Permanent differences, net	328	174
State income tax expense (benefit), net of federal tax	(273)	(173)
Change in valuation allowance	2,142	1,325
Foreign Taxes	-	46
Other	9	4
Total	$243	$171

As of September 30, 2014, the Company has a federal net operating loss (NOL) carryforward of approximately $13 million that expires on various dates through 2034. Internal Revenue Code Section 382 places a limitation on the amount of taxable income which can be offset by NOL carryforwards after a change in control of a loss corporation. Due to these “change of ownership” provisions, utilization of NOL carryforwards may be subject to an annual limitation in future periods. The Company has not performed a Section 382 analysis. However, if performed, Section 382 may be found to limit future utilization of the Company’s NOL carryforwards. The Company also has approximately $8 million in state NOLs which expire on various dates through 2034.

The Company has deferred tax assets that are available to offset future taxable income. A valuation allowance is established if it is more likely than not that all or a portion of the deferred tax assets will not be realized. Management believes that it is more likely than not that all deferred tax assets will not be realized. Accordingly, the Company has established a valuation allowance against a portion of its deferred tax assets at September 30, 2014 and 2013. For the years ended September 30, 2014 and 2013 the valuation allowance for deferred tax assets increased $2,030 and $1,194, respectively which was mainly due to the increase in the net operating loss.

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The Company recognizes interest accrued related to unrecognized tax benefits in interest expense. Penalties, if incurred, are recognized as a component of tax expense.

The Company is subject to U.S. federal income tax as well as income tax of certain state jurisdictions. The Company has not been audited by the Internal Revenue Service (IRS) or any states in connection with income taxes. The tax periods from 2010 to 2014 generally remain open to examination by the IRS and state authorities.

Significant components of the Company's deferred tax assets and liabilities are as follows:

	September 30,	
	2014	**2013**
Deferred tax assets:		
Current:		
Bad debt reserve	$74	$28
Deferred revenue	771	689
Accrued vacation	18	
Long-term		
AMT carryforward	23	9
Net operating loss carryforwards	5,242	3,613
Contribution carryforward	31	-
Total deferred tax assets	6,159	4,339
Deferred tax liabilities:		
Long-term:		
Intangibles	(321)	(102)
Depreciation	(55)	(265)
Total deferred tax liabilities	(376)	(367)
Total deferred tax assets, net, before valuation allowance	5,783	3,972
Valuation allowance	(6,104)	(4,074)
Net deferred tax (liabilities) assets	$(321)	$(102)

Net deferred tax liability is reflected in other long term liabilities on the consolidated balance sheets. Undistributed earnings of the Company's foreign subsidiary amounted to approximately $144 and $376 at September 30, 2014 and 2013, respectively. These earnings are considered to be indefinitely reinvested; accordingly, no provision for US federal and state income taxes has been provided thereon. Upon repatriation of those earnings, in the form of dividends or otherwise, the Company would be subject to both US income taxes (subject to an adjustment for foreign tax credits) and withholding taxes payable to the applicable foreign tax authority. Determination of the amount of unrecognized deferred US income tax liability is not material and the detailed calculations have not been performed. As of September 30, 2014, there would be minimal withholding taxes upon remittance of all previously unremitted earnings.

When accounting for uncertain income tax positions, the impact of uncertain tax positions are recognized in the financial statements if they are more likely than not of being sustained upon examination, based on the technical merits of the position. The Company’s management has determined that the Company has no uncertain tax positions requiring recognition as of September 30, 2014 and 2013.

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14. Earnings per Share

Options to purchase shares of the Company's common stock of 421,131 and 588,108 for fiscal 2014 and 2013, respectively were excluded from the computation of diluted net loss per share as the effect was anti-dilutive to the Company's net loss. Also, excluded were contingent shares issuable in connection with the Magnetic, MarketNet and ElementsLocal acquisitions.

Basic and diluted net loss per share are calculated as follows:

	Year Ended September 30,	
	2014	**2013**
Net loss	$(6,215)	$(3,598)
Basic net loss per share:		
Weighted average common shares outstanding	19,689,930	15,558,244
Basic net loss per share	$(0.32)	$(0.23)
Diluted net loss per share:		
Weighted average common shares outstanding	19,689,930	15,558,244
Weighted average dilutive common share equivalents	-	-
Total weighted average common shares outstanding and dilutive common equivalents	19,689,930	15,558,244
Diluted net loss per share	$(0.32)	$(0.23)

15. Related Party Transactions

On November 1, 2013, Mr. Michael Taglich joined the Board of Directors. Mr. Taglich is the Chairman and President of Taglich Brothers, Inc. a New York based securities firm. Taglich Brothers, Inc. was the agent for the past three private placements of Bridgeline Digital common stock in 2012, 2013, and 2014. Mr. Taglich was also the agent for Bridgeline's convertible debt offerings of $2 million and $1 million in September and November 2013, respectively. Mr. Taglich personally owns 739,029 shares of Bridgeline common stock and 43,478 are held in trust by his wife. He also has 76,293 shares issuable upon conversion of convertible notes and 258,965 shares issuable upon the exercise of warrants. Other employees, affiliates and clients of Taglich Brothers, Inc. own approximately 6,200,000 shares of Bridgeline stock. The fees paid to Taglich Brothers, Inc. in connection with the 2012, 2013, and 2014 private placements of common stock were $651. Fees paid to Taglich Brothers, Inc. in connection with the 2013 convertible debt offerings was $240. The Company also has an annual service contract for $18 with Taglich Brothers, Inc to perform market research.

BRIDGELINE DIGITAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

16. Subsequent Events

Preferred Stock

On October 27, 2014, the Company sold 200,000 shares of convertible preferred stock (the “Preferred Stock”) at purchase price of $10.00 per share for gross proceeds of $2.0 million in a private placement. Net proceeds to the Company after offering expenses were approximately $1.8 million. Each share of Preferred Stock will be convertible into shares of common stock at a conversion price of $0.65 per share. Cumulative dividends are payable in cash quarterly at a rate of 6% per year. If the Company does not pay the dividends in cash, then the Company may pay dividends in any quarter by delivery of additional shares of Preferred Stock (“PIK Election”). If the Company shall make the PIK Election with respect to the dividend payable, it shall deliver a number of shares of Preferred Stock equal to (A) the aggregate dividend payable to such holder as of the end of the quarter divided by (B) the lesser of (x) the then effective Conversion Price or (y) the average VWAP for the five (5) consecutive Trading Days prior to such dividend payment date. If, after two years, any Preferred Stock are outstanding the cash dividend rate will increase to 12.0% per year. The Company shall have the right to force conversion of the Preferred Stock into shares of Common Stock at any time after the Common Stock trades in excess of $1.30 per share. The Preferred Shares shall vote with the Common an as converted basis.

The Placement Agent for the sale was Taglich Brothers, Inc. As fee for the transaction, the Company paid a cash fee of 8% of the transaction. In addition, the Placement Agent shall receive warrants with a five (5) year term for the purchase of an amount of Common Stock equal to ten percent (10.0%) of the number of shares of Common Stock (into which the Preferred Stock are convertible) are sold. The exercise price of the Placement Agent Warrants will equal $0.65 per share.

Related Party

In December 2014, Mr. Michael Taglich, a member of our Board of Directors, signed an unconditional guarantee (the “Guaranty”) and promise to pay the Company’s lender, Bridge Bank, N.A all indebtedness in an amount not to exceed $1,000,000. The Guaranty is cumulative and does not supersede any other outstanding guaranties, and the liability of Mr. Taglich (“Guarantor”) under this Guaranty is exclusive of Guarantor's liability under any other guaranties signed by Guarantor.

Under the terms of the Guaranty, the Guarantor authorizes Lender, without notice or demand and without affecting its liability hereunder, from time to time to: (a) renew, compromise, extend, accelerate, or otherwise change the time for payment, or otherwise change the terms, of the Indebtedness or any part thereof, including increase or decrease of the rate of interest thereon, or otherwise change the terms of the Indebtedness; (b) receive and hold security for the payment of this Guaranty or any Indebtedness and exchange, enforce, waive, release, fail to perfect, sell, or otherwise dispose of any such security; (c) apply such security and direct the order or manner of sale thereof as Lender in its discretion may determine; and (d) release or substitute any Guarantor or any one or more of any endorsers or other guarantors of any of the Indebtedness.

The Guarantor agrees that until the Indebtedness has been paid in full and any commitments of Lender or facilities provided by Lender with respect to the Indebtedness have been terminated, Guarantor shall not be released by or because of the taking, or failure to take, any action that might in any manner or to any extent vary the risks of Guarantor under this Guaranty or that, but for this paragraph, might discharge or otherwise reduce, limit, or modify Guarantor's obligations under this Guaranty. It is the express intent of Guarantor that Guarantor’s obligations under this Guaranty are and shall be absolute and unconditional.

To secure all of Guarantor's obligations hereunder, Guarantor assigns and grants to Lender a security interest in all moneys, securities, and other property of Guarantor now or hereafter in the possession of Lender, all deposit accounts of Guarantor maintained with Lender, and all proceeds thereof. Upon default or breach of any of Guarantor's obligations to Lender, Lender may apply any deposit account to reduce the Indebtedness, and may foreclose any collateral as provided in the Uniform Commercial Code and in any security agreements between Lender and Guarantor.

Line of Credit

In December 2014, the Company signed an Amendment to its Loan and Security Agreement with Bridge Bank. (the “Amendment”). Included in the Amendment is a waiver for financial covenant defaults for the periods of July 2014 through November 2014. The Amendment does not waive any other failure by Borrower to perform its obligations under the Loan Documents. The Amendment also modified certain monthly financial reporting requirements and financial covenants on a prospective basis commencing as of the effective date of the Amendment.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None

Item 9A. Controls and Procedures.

Management's Report on Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed under the *Securities Exchange Act of 1934* , as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our President and Chief Executive Officer (Principal Executive Officer) and our Executive Vice President of Finance and Chief Financial Officer (Principal Financial and Accounting Officer), as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, as ours are designed to do, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of September 30, 2014, the end of our fiscal year covered by this report, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, we concluded that our disclosure controls and procedures were effective as of the end of the period covered by this annual report.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of internal control include providing management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States. Our management assessed the effectiveness of our internal control over financial reporting as of September 30, 2014. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in *Internal Control-Integrated Framework* . Our management has concluded that as of September 30, 2014, our internal control over financial reporting is effective in providing reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with US generally accepted accounting principles. Our management reviewed the results of their assessment with our Board of Directors.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to a permanent exemption from the internal control audit requirements of Section 404(b) of the Sarbanes-Oxley Act of 2002.

Inherent Limitations on Effectiveness of Controls

Internal control over financial reporting has inherent limitations which include but are not limited to the use of independent professionals for advice and guidance, interpretation of existing and/or changing rules and principles, segregation of management duties, scale of organization, and personnel factors. Internal control over financial reporting is a process which involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Provided its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis, however these inherent limitations are known features of the financial reporting process and it is possible to design into the process safeguards to reduce, though not eliminate, this risk. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. 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.

Changes in Internal Control over Financial Reporting

There have been no significant changes in our internal controls over financial reporting that occurred during the fiscal quarter ended September 30, 2014 that have materially or are reasonably likely to materially affect, our internal controls over financial reporting.

Item 9B: Other Information.

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

The following table sets forth information regarding our directors and executive officers:

Name	Age	Position
Thomas Massie	53	Chairman, Chief Executive Officer and President
Kenneth Galaznik	63	Director (1)(4)
Joni Kahn	59	Director (1)(2)(4)
Scott Landers	44	Director(1)(3)(4)
Michael Taglich	59	Director
Brett Zucker	42	Executive Vice President and Chief Technical Officer
Michael Prinn	41	Executive Vice President and Chief Financial Officer

(1) Member of the Audit Committee.
(2) Member of the Compensation Committee.
(3) Member of the Nominating and Governance Committee.
(4) Independent director.

The additional information required by this Item 10 of Form 10-K is hereby incorporated by reference to the information in our definitive proxy statement to be filed within 120 days after the close of our fiscal year.

Item 11. Executive Compensation.

The information required by this Item 11 of Form 10-K is hereby incorporated by reference to the information in our definitive proxy statement to be filed within 120 days after the close of our fiscal year.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

We maintain a number of equity compensation plans for employees, officers, directors and other entities and individuals whose efforts contribute to our success. The table below sets forth certain information as of our fiscal year ended September 30, 2014 regarding the shares of our common stock available for grant or granted under our equity compensation plans.

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)
Equity compensation plans approved by security holders (1)	3,535,640	$ 0.98	1,181,700
Equity compensation plans not approved by security holders (2)	1,508,700	$ 1.25	-
Total	5,044,340	$ 1.06	1,181,700

(1) On April 12, 2012, the Company's stockholders approved and adopted the Bridgeline Digital, Inc. 2012 Employee Stock Purchase Plan for a total of 300,000 shares and 26,548 shares were issued in fiscal 2014. The remaining shares are included in column (c).

(2) At September 30, 2014, there were 1,508,700 total Warrants outstanding.

On October 21, 2010, the Company issued 50,000 common stock warrants to purchase shares of the Company's common stock to a non-employee consultant as compensation for services rendered. The warrants vested over a one year period and expire on October 15, 2015. Of the warrants issued, 25,000 are exercisable at an exercise price of $1.00 per share and 25,000 are exercisable at an exercise price of $2.00 per share.

On May 31, 2012, the Company issued five year warrants to the placement agent in the Company's private placement. The warrants are exercisable to purchase 217,931 shares of the Company's common stock at a price equal to $1.40 per share.

On June 19, 2013, the Company issued five year warrants to the investors and placement agent in the Company’s private placement. The warrants are exercisable to purchase 460,000 and 230,000 shares, respectively, of the Company’s common stock at a price equal to $1.25 per share.

On September 30, 2013, the Company issued five year warrants to the placement agent in the Company's placement of subordinated convertible debt. The warrants are exercisable to purchase 153,846 of the Company's common stock at a price equal to $1.30 per share. The warrants are first exercisable on March 30, 2014, provide the holders piggyback registration rights with respect to the shares of common stock underlying the warrants and contain a cashless exercise provision.

On November 1, 2013, the Company issued five year warrants to the placement agent in the Company's placement of subordinated convertible debt. The warrants are exercisable to purchase 76,923 shares of the Company's common stock at a price equal to $1.30 per share. The warrants are first exercisable on May 6, 2014, provide the holders piggyback registration rights with respect to the shares of common stock underlying the warrants and contain a cashless exercise provision.

On March 28, 2014, the Company issued five year warrants to the investors and placement agent in the Company's private placement. The warrants are exercisable to purchase 320,000 shares of the Company's common stock at a price equal to $1.05 per share.

As of September 30, 2014: (i) placement agent warrants to purchase 217,931, 230,000, 230,769, and 320,000 shares at an exercise price of $1.40, $1.25, $1.30 and $1.05, respectively are outstanding; (ii) investor warrants to purchase 460,000 shares at an exercise price of $1.25, and (iii) warrants issued to a non-employee consultant to purchase 25,000 shares at an exercise price of $1.00 and 25,000 shares at an exercise price of $2.00 are outstanding.

The additional information required by this Item 12 of Form 10-K is hereby incorporated by reference to the information in our definitive proxy statement to be filed within 120 days after the close of our fiscal year.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by this Item 13 of Form 10-K is hereby incorporated by reference to the information in our definitive proxy statement to be filed within 120 days after the close of our fiscal year.

Item 14. Principal Accounting Fees and Services.

The information required by this Item 14 of Form 10-K is hereby incorporated by reference to the information in our definitive proxy statement to be filed within 120 days after the close of our fiscal year.

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PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Documents Filed as Part of this Form 10-K

1. Financial Statements (included in Item 8 of this report on Form 10-K):

– Reports of Independent Registered Public Accounting Firm

– Consolidated Balance Sheets as of September 30, 2014 and 2013

– Consolidated Statements of Operations for the years ending September 30, 2014 and 2013

– Consolidated Statements of Comprehensive Loss for the years ending September 30, 2014 and 2013

– Consolidated Statements of Shareholders' Equity for the years ending September 30, 2014 and 2013

– Consolidated Statements of Cash Flows for the years ending September 30, 2014 and 2013

– Notes to Consolidated Financial Statements

2. Financial Statement Schedules

– Not applicable

(b) Exhibits

Documents listed below, except for documents followed by a parenthetical, are being filed as exhibits. Documents followed by a parenthetical are not being filed herewith and, pursuant to Rule 12b-32 of the General Rules and Regulations promulgated by the SEC under the Securities Exchange Act of 1934 (the Act), reference is made to such documents as previously filed as exhibits with the SEC.

Item	Title
2.1	Asset Purchase Agreement, dated as of May 11, 2010, by and between Bridgeline Digital, Inc. and TMX Interactive, Inc. (incorporated by reference to Exhibit 2.1 to our Quarterly Report on Form 10-Q for the quarter ended March 31, 2010, filed on May 17, 2010)
2.2	Subordinated Promissory Note dated May 11, 2010, issued by Bridgeline Digital, Inc. (incorporated by reference to Exhibit 2.2 to our Quarterly Report on Form 10-Q for the quarter ended March 31, 2010, filed on May 17, 2010)
2.3	Asset Purchase Agreement, dated as of July 9, 2010, by and between Bridgeline Digital, Inc. and e.magination network, LLC. (incorporated by reference to Exhibit 2.1 to our Current Report on Form 8-K filed on July 15, 2010)
2.4	Agreement and Plan of Merger, dated as of October 3, 2011, by and among Bridgeline Digital, Inc., Magnetic Corporation and Jennifer Bakunas (incorporated by reference to Exhibit 2.1 to our Current Report on Form 8-K filed on October 6, 2011)
2.5	Agreement and Plan of Merger, dated as of May 31, 2012, by and among Bridgeline Digital, Inc., MarketNet, Inc. and Jill Bach (incorporated by reference to Exhibit 2.1 to our Current Report on Form 8-K filed on June 5, 2012)
3.1 (i)	Certificate of Amendment to Amended and Restated Certificate of Incorporation, dated March 19, 2010 (incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K filed on March 24, 2010)
3.1 (ii)	Amended and Restated By-laws (incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K filed on January 27, 2011)
4.1	Specimen Common Stock Certificate (incorporated by reference to Exhibit 4.1 to our Registration Statement on Form S-B2, File No. 333-139298)
10.1*	Employment Agreement with Thomas Massie, dated October 1, 2001 (incorporated by reference to Exhibit 10.7 to our Registration Statement on Form S-B2, File No. 333-139298)
10.2*	Employment Agreement with Brett Zucker, dated January 1, 2006 (incorporated by reference to our Quarterly Report on Form 10-Q filed on May 15, 2014)
10.3*	Employment Agreement with Michael D. Prinn, dated January 19, 2011 (incorporated by reference to Exhibit 10.5 to our Quarterly Report Form 10-Q filed on May 15, 2014)
10.4	Form of Warrant to Purchase Common Stock of Bridgeline Digital, Inc., issued to the underwriters (incorporated by reference to Exhibit 10.65 to our Registration Statement on Form S-B2, File No. 333-139298)

10.5	Amended and Restated Stock Incentive Plan, as amended (incorporated by reference to Appendix C to our Revised Definitive Proxy Statement filed on July 14, 2014)*
10.6	Lead Dog Digital, Inc. 2001 Stock Option Plan (incorporated by reference to Exhibit 10.34 to our Registration Statement on Form S-B2, File No. 333-139298)*
10.7	Employee Stock Purchase Plan (incorporated by reference to Appendix C to our Revised Definitive Proxy Statement filed on February 28, 2011)*
10.8	Amended and Restated Loan Agreement dated March 31, 2010, between Bridgeline Digital, Inc. and Silicon Valley Bank (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on April 5, 2010)
10.9	Amended and Restated Intellectual Property Security Agreement dated March 31, 2010, between Bridgeline Digital, Inc. and Silicon Valley Bank (incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K filed on April 5, 2010)
10.10	Fourth Loan Modification Agreement dated May 6, 2011, between Bridgeline Digital, Inc., e.MAGINATION IG, LLC and Silicon Valley Bank (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on May 11, 2011)
10.11	Sixth Loan Modification Agreement dated May 11, 2012 between Bridgeline Digital, Inc., Bridgeline Intelligence Group, Inc. and Silicon Valley Bank (incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q filed on May 14, 2012)
10.12	Securities Purchase Agreement between Bridgeline Digital, Inc. and the investors named therein, dated October 29, 2010 (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on November 4, 2010)
10.13	Form of Common Stock Purchase Warrant issued to Placement Agent, Dated October 29, 2010 (incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K filed on November 4, 2010)
10.14	Securities Purchase Agreement between Bridgeline Digital, Inc. and the investors named therein, dated May 31, 2012 (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on June 5, 2012)
10.15	Form of Common Stock Purchase Warrant issued to Placement Agent, dated May 31, 2012 (incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K filed on June 5, 2012)
10.16	Amendment to Note Purchase Agreement between Bridgeline Digital, Inc. and the investors named therein, dated November 6, 2013 (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on November 6, 2013).
10.17	Form of Promissory Note issued to Investors, dated November 6, 2013 (incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K filed on November 6, 2013).
10.18	Form of Common Stock Purchase Warrant issued to Placement Agent, dated November 6, 2013 (incorporated by reference to Exhibit 10.3 to our Current Report on Form 8-K filed on November 6, 2013).
10.19	First Amendment to the Security Agreement made by Bridgeline Digital, Inc. in favor of Taglich Brothers, Inc. in its capacity as collateral agent for the lenders named therein, dated November 6, 2013 (incorporated by reference to Exhibit 10.4 to our Current Report on Form 8-K filed on November 6, 2013).
10.20	Placement Agent Agreement between Bridgeline Digital, Inc. and Taglich Brothers, Inc., dated October 30, 2013 (incorporated by reference to Exhibit 10.5 to our Current Report on Form 8-K filed November 6, 2013).
10.21	Bridgeline Digital, Inc. and Bridge Bank, National Association Loan and Security Agreement dated December 20, 2013 (incorporated by reference to Exhibit 10.6 to our Quarterly Report on Form 10-Q filed on February 14, 2014).

10.22	Form of Restricted Stock Agreement by and between Bridgeline Digital, Inc. and certain Board of Directors dated February 24, 2014 (incorporated by reference to Exhibit 10.2 to our Quarterly Report on Form 10-Q filed on May 15, 2014).
10.23	Securities Purchase Agreement between Bridgeline Digital, Inc. and the Investors named therein dated March 28, 2014 (incorporated by reference to Exhibit 10.3 to our Quarterly Report on Form 10-Q filed on May 15, 2014).
10.24	Form of Common Stock Purchase Warrant issued to Placement Agent, dated March 28, 2014 (incorporated by reference to Exhibit 10.4 our Quarterly Report on Form 10-Q filed on May 15, 2014).
10.25	Loan and Security Modification Agreement
10.26	Bridge Bank Guaranty
21.1	Subsidiaries of the Registrant
23.1	Consent of Marcum LLP
31.1	CEO Certification, Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	CFO Certification, Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	CEO Certification, Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	CFO Certification, Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS**	XBRL Instance
101.SCH**	XBRL Taxonomy Extension Schema
101.CAL**	XBRL Taxonomy Extension Calculation
101.DEF**	XBRL Taxonomy Extension Definition
101.LAB**	XBRL Taxonomy Extension Labels
101.PRE**	XBRL Taxonomy Extension Presentation

*	Management compensatory plan
**	XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

(c) Financial Statement Schedules

Not applicable

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BRIDGELINE DIGITAL, INC.
a Delaware corporation

By: /s/ Thomas Massie

Name: Thomas Massie

December 29, 2014

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Thomas Massie Thomas Massie	Chief Executive Officer and Director (Principal Executive Officer)	December 29, 2014
/s/ Michael Prinn Michael Prinn	Chief Financial Officer (Principal Financial Officer)	December 29, 2014
/s/Kenneth Galaznik Kenneth Galaznik	Director	December 29, 2014
/s/ Joni Kahn Joni Kahn	Director	December 29, 2014

/s/ Scott Landers Director December 29, 2014
Scott Landers

/s/ Michael Taglich Director December 29, 2014
Michael Taglich

Index of Exhibits

Exhibit No.	Description of Document
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101.INS*	XBRL Instance
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101.CAL*	XBRL Taxonomy Extension Calculation
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101.LAB*	XBRL Taxonomy Extension Labels
101.PRE*	XBRL Taxonomy Extension Presentation

*XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.