BLACKBAUD INC
Form 10-Q
May 06, 2015

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

FORM 10-Q

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

For the quarterly period ended March 31, 2015

or

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

For the transition period from to .

Commission file number: 000-50600

Blackbaud, Inc.

(Exact name of registrant as specified in its charter)

Delaware	11-2617163
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2000 Daniel Island Drive
Charleston, South Carolina 29492
(Address of principal executive offices, including zip code)
(843) 216-6200
(Registrant's telephone number, including area code)

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

YES þ 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 (Section 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 þ NO ¨

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

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

Indicate by check mark whether registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES ¨ NO þ

The number of shares of the registrant's Common Stock outstanding as of April 27, 2015 was 46,873,670.

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Blackbaud, Inc.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains “forward-looking statements” that anticipate results based on our estimates, assumptions and plans that are subject to uncertainty. These statements are made subject to the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements in this report not dealing with historical results or current facts are forward-looking and are based on estimates, assumptions and projections. Statements which include the words “believes,” “seeks,” “expects,” “may,” “might,” “should,” “intends,” “could,” “would,” “likely,” “will,” “targets,” “p “aims,” “projects,” “estimates” or the negative version of those words and similar statements of a future or forward-looking nature identify forward-looking statements.

Although we attempt to be accurate in making these forward-looking statements, future circumstances might differ from the assumptions on which such statements are based. In addition, other important factors that could cause results to differ materially include those set forth elsewhere in this report, under “Item 1A. Risk factors” and elsewhere in our Annual Report on Form 10-K for the year ended December 31, 2014 and in our other SEC filings. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
Blackbaud, Inc.
Consolidated balance sheets
(Unaudited)

(in thousands, except share amounts)	March 31, 2015	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$13,286	$14,735
Donor restricted cash	58,355	140,709
Accounts receivable, net of allowance of $4,393 and $4,539 at March 31, 2015 and December 31, 2014, respectively	74,901	77,523
Prepaid expenses and other current assets	39,074	40,392
Deferred tax asset, current portion	14,119	14,423
Total current assets	199,735	287,782
Property and equipment, net	47,444	50,402
Goodwill	348,605	349,008
Intangible assets, net	220,910	229,307
Other assets	26,668	26,684
Total assets	$843,362	$943,183
Liabilities and stockholders' equity		
Current liabilities:		
Trade accounts payable	$11,203	$11,436
Accrued expenses and other current liabilities	35,270	52,201
Donations payable	58,355	140,709
Debt, current portion	4,375	4,375
Deferred revenue, current portion	205,876	212,283
Total current liabilities	315,079	421,004
Debt, net of current portion	281,413	276,196
Deferred tax liability	42,443	43,639
Deferred revenue, net of current portion	9,102	8,991
Other liabilities	7,445	7,437
Total liabilities	655,482	757,267
Commitments and contingencies (see Note 12)		
Stockholders' equity:		
Preferred stock; 20,000,000 shares authorized, none outstanding	—	—
Common stock, $0.001 par value; 180,000,000 shares authorized, 56,641,530 and 56,048,135 shares issued at March 31, 2015 and December 31, 2014, respectively	57	56
Additional paid-in capital	251,340	245,674
Treasury stock, at cost; 9,775,789 and 9,740,054 shares at March 31, 2015 and December 31, 2014, respectively	(192,038)	(190,440)
Accumulated other comprehensive loss	(1,827)	(1,032)
Retained earnings	130,348	131,658
Total stockholders' equity	187,880	185,916
Total liabilities and stockholders' equity	$843,362	$943,183

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

Blackbaud, Inc.
Consolidated statements of comprehensive income
(Unaudited)

(in thousands, except share and per share amounts)	Three months ended March 31, 2015	2014
Revenue		
Subscriptions	$72,513	$58,268
Maintenance	38,896	35,652
Services	31,306	28,130
License fees and other	4,278	5,572
Total revenue	146,993	127,622
Cost of revenue		
Cost of subscriptions	36,178	30,124
Cost of maintenance	7,502	5,414
Cost of services	26,971	26,263
Cost of license fees and other	1,161	1,529
Total cost of revenue	71,812	63,330
Gross profit	75,181	64,292
Operating expenses		
Sales and marketing	28,562	25,116
Research and development	21,276	16,494
General and administrative	16,843	12,818
Amortization	488	587
Total operating expenses	67,169	55,015
Income from operations	8,012	9,277
Interest income	8	16
Interest expense	(1,686)	(1,459)
Loss on debt extinguishment and termination of derivative instruments (see Notes 10 and 11)	—	(996)
Other expense, net	(295)	(236)
Income before provision for income taxes	6,039	6,602
Income tax provision	1,754	2,788
Net income	$4,285	$3,814
Earnings per share		
Basic	$0.09	$0.08
Diluted	$0.09	$0.08
Common shares and equivalents outstanding		
Basic weighted average shares	45,529,668	45,127,645
Diluted weighted average shares	46,168,096	45,552,451
Dividends per share	$0.12	$0.12
Other comprehensive (loss) income		
Foreign currency translation adjustment	(326)	555
Unrealized (loss) gain on derivative instruments, net of tax	(469)	312
Total other comprehensive (loss) income	(795)	867
Comprehensive income	$3,490	$4,681

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

Blackbaud, Inc.
Consolidated statements of cash flows
(Unaudited)

	Three months ended March 31,	
(in thousands)	2015	2014
Cash flows from operating activities		
Net income	$4,285	$3,814
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,678	10,674
Provision for doubtful accounts and sales returns	1,358	1,074
Stock-based compensation expense	5,102	3,714
Excess tax benefits from exercise and vesting of stock-based compensation	(584)	(603)
Deferred taxes	(886)	616
Loss on debt extinguishment and termination of derivative instruments	—	996
Amortization of deferred financing costs and discount	210	162
Other non-cash adjustments	524	168
Changes in operating assets and liabilities, net of acquisition of businesses:		
Accounts receivable	555	2,676
Prepaid expenses and other assets	3,633	309
Trade accounts payable	(111)	2,789
Accrued expenses and other liabilities	(18,768)	(4,158)
Donor restricted cash	82,140	63,680
Donations payable	(82,140)	(63,680)
Deferred revenue	(4,765)	(8,967)
Net cash provided by operating activities	4,231	13,264
Cash flows from investing activities		
Purchase of property and equipment	(2,521)	(6,119)
Purchase of net assets of acquired companies, net of cash acquired	—	(136)
Capitalized software development costs	(3,129)	(1,152)
Net cash used in investing activities	(5,650)	(7,407)
Cash flows from financing activities		
Proceeds from issuance of debt	41,800	196,000
Payments on debt	(36,694)	(173,908)
Debt issuance costs	—	(2,484)
Proceeds from exercise of stock options	11	25
Excess tax benefits from from exercise and vesting of stock-based compensation	584	603
Dividend payments to stockholders	(5,626)	(5,537)
Net cash provided by financing activities	75	14,699
Effect of exchange rate on cash and cash equivalents	(105)	105
Net (decrease) increase in cash and cash equivalents	(1,449)	20,661
Cash and cash equivalents, beginning of period	14,735	11,889
Cash and cash equivalents, end of period	$13,286	$32,550

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

Blackbaud, Inc.
Consolidated statements of stockholders' equity
(Unaudited)

(in thousands, except share amounts)	Common stock		Additional paid-in capital	Treasury stock	Accumulated other comprehensive loss	Retained earnings	Total stockholders' equity
	Shares	Amount					
Balance at December 31, 2013	55,699,817	$ 56	$ 220,763	$(183,288)	$ (1,385)	$125,398	$ 161,544
Net income	—	—	—	—	—	28,290	28,290
Payment of dividends	—	—	—	—	—	(22,107)	(22,107)
Exercise of stock options and stock appreciation rights and vesting of restricted stock units	186,473	—	188	—	—	—	188
Surrender of 166,952 shares upon vesting of restricted stock and restricted stock units and exercise of stock appreciation rights	—	—	—	(7,152)	—	—	(7,152)
Excess tax benefits from exercise and vesting of stock-based compensation	—	—	7,455	—	—	—	7,455
Stock-based compensation	—	—	17,268	—	—	77	17,345
Restricted stock grants	248,567	—	—	—	—	—	—
Restricted stock cancellations	(86,722)	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	353	—	353
Balance at December 31, 2014	56,048,135	$ 56	$ 245,674	$(190,440)	$ (1,032)	$131,658	$ 185,916
Net income	—	—	—	—	—	4,285	4,285
Payment of dividends	—	—	—	—	—	(5,626)	(5,626)
Exercise of stock options and stock appreciation rights and vesting of restricted stock units	88,021	—	11	—	—	—	11
Surrender of 35,735 shares upon vesting of restricted stock and restricted stock units and exercise of stock appreciation rights	—	—	—	(1,598)	—	—	(1,598)
Excess tax benefits from exercise and vesting of stock-based compensation	—	—	584	—	—	—	584
Stock-based compensation	—	—	5,071	—	—	31	5,102
Restricted stock grants	540,155	1	—	—	—	—	1
Restricted stock cancellations	(34,781)	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	(795)	—	(795)
Balance at March 31, 2015	56,641,530	$ 57	$ 251,340	$(192,038)	$ (1,827)	$130,348	$ 187,880

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

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Blackbaud, Inc.
Notes to consolidated financial statements
(Unaudited)

1. Organization

We provide software and services for the nonprofit, charitable giving and education communities. Our offerings include a full spectrum of cloud-based and on-premise solutions, and related services for organizations of all sizes, including nonprofit fundraising and relationship management, marketing, advocacy, accounting, payments and analytics, as well as grant management, corporate social responsibility, education and other solutions. As of March 31, 2015, we had more than 30,000 active customers including nonprofits, K12 private and higher education institutions, healthcare organizations, foundations and other charitable giving entities, and corporations.

2. Summary of significant accounting policies

Unaudited interim consolidated financial statements

The accompanying interim consolidated financial statements have been prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission ("SEC") for interim financial reporting. These consolidated statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary to state fairly the consolidated balance sheets, consolidated statements of comprehensive income, consolidated statements of cash flows and consolidated statements of stockholders' equity, for the periods presented in accordance with accounting principles generally accepted in the United States ("GAAP"). The consolidated balance sheet at December 31, 2014, has been derived from the audited consolidated financial statements at that date. Operating results and cash flows for the three months ended March 31, 2015 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2015, or any other future period. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with GAAP have been omitted in accordance with the rules and regulations for interim reporting of the SEC. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2014, and other forms filed with the SEC from time to time.

Reclassifications

In order to provide comparability between periods presented, "license fees" and "other revenue" have been combined within "license fees and other" in the previously reported consolidated statements of comprehensive income to conform to presentation of the current period. Similarly, "cost of license fees" and "cost of other revenue" have been combined within "cost of license fees and other" in the previously reported consolidated statements of comprehensive income to conform to presentation of the current period.

Reclassifications were also made to prior period segment disclosures to reflect a change in reportable segments including the reassignment of goodwill from a former reportable segment to the other reportable segments. See Note 16 to these consolidated financial statements for additional discussion.

Basis of consolidation

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

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Blackbaud, Inc.
Notes to consolidated financial statements (continued)
(Unaudited)

Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting periods. On an ongoing basis, we reconsider and evaluate our estimates and assumptions, including those that impact revenue recognition, long-lived and intangible assets including goodwill, stock-based compensation, the provision for income taxes, deferred taxes, capitalization of software development costs, our allowances for sales returns and doubtful accounts, deferred sales commissions and professional services costs, valuation of derivative instruments, accounting for business combinations and loss contingencies. Changes in the facts or circumstances underlying these estimates could result in material changes and actual results could materially differ from these estimates.

Revenue recognition

Our revenue is primarily generated from the following sources: (i) charging for the use of our software products in a hosted environment; (ii) providing software maintenance and support services; (iii) providing professional services including implementation, training, consulting, analytic, hosting and other services; and (iv) selling perpetual licenses of our software products.

We recognize revenue when all of the following conditions are met:

•Persuasive evidence of an arrangement exists;
•The products or services have been delivered;
•The fee is fixed or determinable; and
•Collection of the resulting receivable is probable.

Determining whether and when these criteria have been met can require significant judgment and estimates. We deem acceptance of an agreement to be evidence of an arrangement. Delivery of our services occurs when the services have been performed. Delivery of our products occurs when the product is shipped or transmitted, and title and risk of loss have transferred to the customers. Our typical agreements do not include customer acceptance provisions; however, if acceptance provisions are provided, delivery is deemed to occur upon acceptance. We consider the fee to be fixed or determinable unless the fee is subject to refund or adjustment or is not payable within our standard payment terms. Payment terms greater than 90 days are considered to be beyond our customary payment terms. Collection is deemed probable if we expect that the customer will be able to pay amounts under the arrangement as they become due. If we determine that collection is not probable, we defer revenue recognition until collection. Revenue is recognized net of sales returns and allowances.

We follow guidance provided in ASC 605-45, Principal Agent Considerations, which states that determining whether a company should recognize revenue based on the gross amount billed to a customer or the net amount retained is a matter of judgment that depends on the facts and circumstances of the arrangement and that certain factors should be considered in the evaluation.

Subscriptions

We make certain of our software products available for use in hosted application arrangements without licensing perpetual rights to the software (“hosted applications”). Revenue from hosted applications is recognized ratably beginning on the activation date over the term of the agreement, which generally ranges from one to three years. Any revenue related to upfront activation or set-up fees is deferred and recognized ratably over the estimated period that the customer benefits from the related hosted application. Direct and incremental costs related to upfront activation or set-up activities for hosted applications are capitalized until the hosted application is deployed and in use, and then expensed ratably over the estimated period that the customer benefits from the related hosted application.

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Blackbaud, Inc.
Notes to consolidated financial statements (continued)
(Unaudited)

We provide hosting services to customers who have purchased perpetual rights to certain of our software products ("hosting services"). Revenue from hosting services, as well as data enrichment services, data management services and online training programs, is recognized ratably beginning on the activation date over the term of the agreement, which generally ranges from one to three years. Any related set-up fees are recognized ratably over the estimated period that the customer benefits from the related hosting service. The estimated period of benefit is evaluated on an annual basis using historical customer retention information by product or service.

For arrangements that have multiple elements and do not include software licenses, we allocate arrangement consideration at the inception of the arrangement to those elements that qualify as separate units of accounting. The arrangement consideration is allocated to the separate units of accounting based on relative selling price method in accordance with the selling price hierarchy, which includes: (i) vendor specific objective evidence ("VSOE") of fair value if available; (ii) third-party evidence ("TPE") if VSOE is not available; and (iii) best estimate of selling price ("BESP") if neither VSOE nor TPE is available. In general, we use VSOE to allocate the selling price to subscription and service deliverables.

We offer certain payment processing services with the assistance of third-party vendors. In general, when we are the principal in a transaction based on the predominant weighting of factors identified in ASC 605-45, we record the revenue and related costs on a gross basis. Otherwise, we net the cost of revenue associated with the service against the gross amount billed to the customer and record the net amount as revenue.

Revenue from transaction processing services is recognized when the service is provided and the amounts are determinable. Revenue directly associated with processing donations for customers are included in subscriptions revenue.

Maintenance

We recognize revenue from maintenance services ratably over the contract term, typically one year. Maintenance contracts are at rates that vary according to the level of the maintenance program associated with the software product and are generally renewable annually. Maintenance contracts may also include the right to unspecified product upgrades on an if-and-when available basis. Certain support services are sold in prepaid units of time and recognized as revenue upon their usage.

Services

We generally bill consulting, installation and implementation services based on hourly rates plus reimbursable travel-related expenses. Revenue is recognized for these services over the period the services are delivered.

We recognize analytic services revenue from donor prospect research engagements, the sale of lists of potential donors, benchmarking studies and data modeling service engagements upon delivery. In arrangements where we provide customers the right to updates to the lists during the contract period, revenue is recognized ratably over the contract period.

We sell fixed-rate programs, which permit customers to attend unlimited training over a specified contract period, typically one year, subject to certain restrictions, and revenue in those cases is recognized ratably over the contract period. Additionally, we sell training at a fixed rate for each specific class at a per attendee price or at a packaged price for several attendees, and recognize the related revenue upon the customer attending and completing training.

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Blackbaud, Inc.
Notes to consolidated financial statements (continued)
(Unaudited)

License fees

We sell perpetual software licenses with maintenance, varying levels of professional services and, in certain instances, with hosting services. We allocate revenue to each of the elements in these arrangements using the residual method under which we first allocate revenue to the undelivered elements, typically the non-software license components, based on VSOE of fair value of the various elements. We determine VSOE of fair value of the various elements using different methods. VSOE of fair value for maintenance services associated with software licenses is based upon renewal rates stated in the agreements with customers, which demonstrate a consistent relationship of maintenance pricing as a percentage of the contractual license fee. VSOE of fair value of professional services and other products and services is based on the average selling price of these same products and services to other customers when sold on a stand-alone basis. Any remaining revenue is allocated to the delivered elements, which is normally the software license in the arrangement. In general, revenue is recognized for software licenses upon delivery to our customers. When a software license is sold with software customization services, generally the services are to provide the customer assistance in creating special reports and other enhancements that will improve operational efficiency and/or help to support business process improvements. These services are generally not essential to the functionality of the software and the related revenues are recognized either as the services are delivered or upon completion. However, when software customization services are considered essential to the functionality of the software, we recognize revenue for both the software license and the services using the percentage-of-completion method.

Deferred revenue

To the extent that our customers are billed for the above described products and services in advance of delivery, we record such amounts in deferred revenue.

Fair value measurements

We measure certain financial assets and liabilities at fair value on a recurring basis, including derivative instruments. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date. An active market is defined as a market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. We use a three-tier fair value hierarchy to measure fair value. This hierarchy prioritizes the inputs into three broad levels as follows:

- Level 1 - Quoted prices for identical assets or liabilities in active markets;
- Level 2 - Quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets in markets that are not active, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets; and
- Level 3 - Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

Our financial assets and liabilities are classified in their entirety within the hierarchy based on the lowest level of input that is significant to fair value measurement. Changes to a financial asset's or liability's level within the fair value hierarchy are determined as of the end of a reporting period. All methods of assessing fair value result in a general approximation of value, and such value may never actually be realized.

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Blackbaud, Inc.
Notes to consolidated financial statements (continued)
(Unaudited)

Earnings per share

We compute basic earnings per share by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income available to common stockholders by the weighted average number of common shares and dilutive potential common shares outstanding during the period. Diluted earnings per share reflect the assumed exercise, settlement and vesting of all dilutive securities using the “treasury stock method” except when the effect is anti-dilutive. Potentially dilutive securities consist of shares issuable upon the exercise of stock options, settlement of stock appreciation rights and vesting of restricted stock awards and units.

Recently issued accounting pronouncements

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-05, Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40) - Customer's Accounting for Fees Paid in a Cloud Computing Arrangement (ASU 2015-05). The amendments in this update provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, the update specifies that the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. The update further specifies that the customer should account for a cloud computing arrangement as a service contract if the arrangement does not include a software license. ASU 2015-05 will be effective for the Company in fiscal year 2016. Early adoption is permitted. An entity can elect to adopt the amendments either (1) prospectively to all arrangements entered into or materially modified after the effective date or (2) retrospectively. We are currently evaluating implementation methods and the extent of the impact that implementation of this standard will have upon adoption.

In April 2015, the FASB issued ASU 2015-03, Interest - Imputation of Interest - Simplifying the Presentation of Debt Issuance Costs. ASU 2015-03 sets forth a requirement that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs is not affected by the amendments in this update. ASU 2015-03 will be effective for the Company in fiscal year 2016. Early adoption is permitted. An entity should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented is adjusted to reflect the period-specific effects of applying the new guidance. We are currently evaluating the extent of the impact that implementation of this standard will have on adoption; however, we will reclassify debt issuance costs from other assets and record them as a direct deduction from the carrying amount of our debt liability.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and will replace most existing revenue recognition guidance in GAAP when it becomes effective. ASU 2014-09 is effective for fiscal years and interim periods within those years beginning after December 15, 2016. Early adoption is not permitted. An entity should apply ASU 2014-09 either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the ASU recognized as an adjustment to the opening balance of retained earnings at the date of initial application. On April 29, 2015, the FASB issued a proposed ASU to defer the effective date of the new standard for one year. The proposal would now require application of the new standard no later than annual reporting periods beginning after December 15, 2017, including interim reporting periods therein; however, under the proposal, public entities would be permitted to elect to early adopt the new standard as of the original effective date. We expect the adoption of ASU 2014-09 will impact our consolidated financial statements. We are currently evaluating implementation methods and the extent of the impact that implementation of this standard will have upon adoption.

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Blackbaud, Inc.
Notes to consolidated financial statements (continued)
(Unaudited)

3. Business combinations

2014 Acquisitions

MicroEdge

On October 1, 2014, we completed our acquisition of all of the outstanding equity, including all voting equity interests of MicroEdge Holdings, LLC (“MicroEdge”). MicroEdge is a provider of high-performance solutions that enable the worldwide giving community to organize, simplify and measure their acts of charitable giving. The acquisition of MicroEdge expands our offerings in the philanthropic giving sector with MicroEdge’s comprehensive technology solutions for grant-making, corporate social responsibility and foundation management. We acquired MicroEdge for an aggregate purchase price of $159.8 million in cash. As a result of the acquisition, MicroEdge has become a wholly-owned subsidiary of ours. The operating results of MicroEdge have been included in our consolidated financial statements from the date of acquisition within the Enterprise Customer Business Unit. For the three months ended March 31, 2015, MicroEdge's total revenue was $6.6 million. Because we have integrated a substantial amount of MicroEdge's operations, it is impracticable to determine the operating costs attributable solely to the acquired business. We financed the acquisition of MicroEdge through cash on hand and borrowings of $140 million under our existing credit facility.

The preliminary purchase price allocation is based upon a preliminary valuation of assets and liabilities and the estimates and assumptions are subject to change as we obtain additional information during the measurement period, which may be up to one year from the acquisition date. The assets and liabilities pending finalization include the valuation of acquired intangible assets, the assumed deferred revenue and the evaluation of deferred income taxes. Differences between the preliminary and final valuation could have a material impact on our future results of operations and financial position. The following table summarizes the allocation of the purchase price based on the estimated fair value of the assets acquired and the liabilities assumed:

(in thousands)	
Net working capital, excluding deferred revenue	$9,642
Property and equipment	1,371
Other long term assets	792
Deferred revenue	(11,670)
Deferred tax liability	(6,090)
Intangible assets and liabilities	90,200
Goodwill	75,541
Total purchase price	$159,786

The estimated fair value of accounts receivable acquired approximates the contractual value of $6.3 million. The estimated goodwill recognized is attributable primarily to the opportunities for expected synergies from combining operations and the assembled workforce of MicroEdge, all of which was assigned to our Enterprise Customer Business Unit reporting segment. Approximately $34.9 million of the goodwill arising in the acquisition is deductible for income tax purposes.

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Blackbaud, Inc.
Notes to consolidated financial statements (continued)
(Unaudited)

The MicroEdge acquisition resulted in the identification of the following identifiable intangible assets:

MicroEdge	Intangible assets acquired (in thousands)	Weighted average amortization period (in years)
Customer relationships	$61,200	13
Marketing assets	2,500	7
Marketing assets	1,600	Indefinite
Acquired technology	24,300	7
Non-compete agreements	600	3
Total intangible assets	$90,200	11

The estimated fair values of the finite-lived intangible assets was based on variations of the income approach, which estimates fair value based on the present value of cash flows that the assets are expected to generate which included the relief-from-royalty method, incremental cash flow method, excess earnings method and with and without method, depending on the intangible asset being valued. Customer relationships are amortized on an accelerated basis. Marketing assets, certain of the acquired technology and non-compete agreements are being amortized on a straight-line basis. Certain of the acquired technology is being amortized on an accelerated basis.

The following unaudited pro forma condensed combined consolidated results of operations assume that the acquisition of MicroEdge occurred on January 1, 2013. This unaudited pro forma financial information does not reflect any adjustments for anticipated synergies resulting from the acquisition and should not be relied upon as being indicative of the historical results that would have been attained had the transaction been consummated as of January 1, 2013, or of the results that may occur in the future. The unaudited pro forma information reflects adjustments for amortization of intangibles related to the fair value adjustments of the assets acquired, write-down of acquired deferred revenue to fair value, additional interest expense related to the financing of the transaction and the related tax effects of the adjustments.

(in thousands, except per share amounts)	Three months ended March 31, 2014
Revenue	$132,307
Net income	$1,876
Basic earnings per share	$0.04
Diluted earnings per share	$0.04

WhippleHill

On June 16, 2014, we acquired all of the outstanding stock of WhippleHill Communications, Inc. (“WhippleHill”), a privately held company based in New Hampshire, for $35.0 million in cash, subject to certain adjustments set forth in the stock purchase agreement. WhippleHill is a provider of cloud-based solutions designed exclusively to serve K12 private schools. The acquisition of WhippleHill expanded our offerings in the K12 technology sector. The operating results of WhippleHill have been included in our consolidated financial statements from the date of acquisition. Because we have integrated WhippleHill's operations, it is impracticable to determine the revenue and operating costs attributable solely to the acquired business.

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We recorded $22.2 million of finite-lived intangible assets, $9.3 million of goodwill (all of which is deductible for income tax purposes) and $3.5 million of net tangible assets acquired and liabilities assumed associated with this acquisition based on our preliminary determination of estimated fair values. Included in net tangible assets acquired and liabilities assumed was $4.6 million of acquired accounts receivable, for which fair value was estimated to approximate the contractual value. The assets and liabilities recorded for the acquisition of WhippleHill were based on preliminary valuations and the estimates and assumptions are subject to change as we obtain additional information during the measurement period, which may be up to one year from the acquisition date. The assets and liabilities pending finalization include the valuation of acquired intangible assets, the assumed deferred revenue and the evaluation of deferred income taxes. Differences between the preliminary and final valuation could have a material impact on our future results of operations and financial position. The estimated goodwill recognized is attributable primarily to the opportunities for expected synergies from combining operations and the assembled workforce of WhippleHill, all of which was assigned to our General Markets Business Unit reporting segment.

The WhippleHill acquisition resulted in the identification of the following identifiable finite-lived intangible assets:

WhippleHill	Intangible assets acquired (in thousands)	Weighted average amortization period (in years)
Customer relationships	$11,300	11
Acquired technology	8,500	7
Marketing assets	2,300	9
Non-compete agreements	100	3
Total intangible assets	$22,200	9

The estimated fair values of the finite-lived intangible assets were based on variations of the income approach which estimates fair value based upon the present value of cash flows that the assets are expected to generate and which included the relief-from-royalty method, incremental cash flow method, excess earnings method and with and without method, depending on the intangible asset being valued. Customer relationships are being amortized on an accelerated basis. Acquired technology, trade names and non-compete agreements are being amortized on a straight-line basis.

We determined that the WhippleHill acquisition was a non-material business combination. As such, pro forma disclosures are not required and are not presented.

4. Earnings per share

The following table sets forth the computation of basic and diluted earnings per share:

	Three months ended March 31,	
(in thousands, except share and per share amounts)	2015	2014
Numerator:		
Net income	$4,285	$3,814
Denominator:		
Weighted average common shares	45,529,668	45,127,645
Add effect of dilutive securities:		
Stock-based compensation	638,428	424,806
Weighted average common shares assuming dilution	46,168,096	45,552,451
Earnings per share:		
Basic	$0.09	$0.08

Diluted	$0.09	$0.08

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Blackbaud, Inc.
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The following shares underlying stock-based awards were not included in diluted earnings per share because their inclusion would have been anti-dilutive:

	Three months ended March 31,	
	2015	2014
Shares excluded from calculations of diluted earnings per share	18,575	351,383

5. Fair value measurements

Recurring fair value measurements

Financial assets and liabilities measured at fair value on a recurring basis consisted of the following, as of:

	Fair value measurement using			
(in thousands)	Level 1	Level 2	Level 3	Total
Fair value as of March 31, 2015				
Financial liabilities:				
Derivative instruments[(1)]	$—	$1,030	$—	$1,030
Total financial liabilities	$—	$1,030	$—	$1,030
Fair value as of December 31, 2014				
Financial liabilities:				
Derivative instruments[(1)]	$—	$268	$—	$268
Total financial liabilities	$—	$268	$—	$268

(1) The fair value of our interest rate swaps was based on model-driven valuations using LIBOR rates, which are observable at commonly quoted intervals. Accordingly, our interest rate swaps are classified within Level 2 of the fair value hierarchy.

We believe the carrying amounts of our cash and cash equivalents, donor restricted cash, accounts receivable, trade accounts payable, accrued expenses and other current liabilities and donations payable approximate their fair values at March 31, 2015 and December 31, 2014, due to the immediate or short-term maturity of these instruments.

We believe the carrying amount of our debt approximates its fair value at March 31, 2015 and December 31, 2014, as the debt bears interest rates that approximate market value. As LIBOR rates are observable at commonly quoted intervals, it is classified within Level 2 of the fair value hierarchy.

Non-recurring fair value measurements

Assets and liabilities that are measured at fair value on a non-recurring basis include intangible assets and goodwill which are recognized at fair value during the period in which an acquisition is completed, from updated estimates and assumptions during the measurement period, or when they are considered to be impaired. These non-recurring fair value measurements, primarily for intangible assets acquired, were based on Level 3 unobservable inputs. In the event of an impairment, we determine the fair value of the goodwill and intangible assets using a discounted cash flow approach, which contains significant unobservable inputs and therefore is considered a Level 3 fair value measurement. The unobservable inputs in the analysis generally include future cash flow projections and a discount rate.

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6. Goodwill and other intangible assets

The change in goodwill for each reportable segment (as defined in Note 16) during the three months ended March 31, 2015, consisted of the following:

(in thousands)	ECBU	GMBU	IBU	Other[1]	Total
Balance at December 31, 2014	$240,621	$99,806	$6,485	$2,096	$349,008
Effect of foreign currency translation	—	—	(403)	—	(403)
Balance at March 31, 2015	$240,621	$99,806	$6,082	$2,096	$348,605

(1) Other includes goodwill not assigned to one of our three reportable segments.

As a result of the change in our reportable segments as of March 31, 2015, $33.2 million of goodwill that had been attributed to the former Target Analytics segment was reassigned. Of that amount $17.3 million, $15.6 million and $0.3 million was reassigned to ECBU, GMBU and IBU, respectively, based on their relative fair values. The reassignment of goodwill is reflected in the goodwill balances as of March 31, 2015 and December 31, 2014. In connection with the change in reportable segments, goodwill allocated to the ECBU, GMBU and IBU reporting units was reviewed under the two-step quantitative goodwill impairment test in accordance with the authoritative guidance. Under the first step of the authoritative guidance for impairment testing, the fair value of the reporting units was determined based on the income approach, which estimates the fair value based on the future discounted cash flows. Based on the first step of the analysis, we determined the fair value of each reporting unit is significantly above its respective carrying amount. As such, we were not required to perform step two of the analysis for the purposes of determining the amount of any impairment loss and no impairment charge was recorded as a result of the interim period impairment test performed during the three months ended March 31, 2015.

Amortization expense

Amortization expense related to finite-lived intangible assets acquired in business combinations is allocated to cost of revenue on the consolidated statements of comprehensive income based on the revenue stream to which the asset contributes, except for marketing assets and non-compete agreements, for which the associated amortization expense is included in operating expenses. The following table summarizes amortization expense:

	Three months ended March 31,	
(in thousands)	2015	2014
Included in cost of revenue:		
Cost of subscriptions	$5,772	$4,560
Cost of maintenance	1,153	115
Cost of services	607	656
Cost of license fees and other	107	106
Total included in cost of revenue	7,639	5,437
Included in operating expenses	488	587
Total amortization of intangibles from business combinations	$8,127	$6,024

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The following table outlines the estimated future amortization expense for each of the next five years for our finite-lived intangible assets as of March 31, 2015:

Year ending December 31, (in thousands)	Amortization expense
2015 - remaining	$24,237
2016	34,878
2017	32,282
2018	30,172
2019	27,124
Total	$148,693

7. Prepaid expenses and other assets

Prepaid expenses and other assets consisted of the following as of:

(in thousands)	March 31, 2015	December 31, 2014
Deferred sales commissions	$21,173	$22,630
Prepaid software maintenance	9,411	9,480
Taxes, prepaid and receivable	6,596	8,991
Deferred professional services costs	5,229	5,753
Software development costs	11,268	8,914
Prepaid royalties	2,858	3,192
Other assets	9,207	8,116
Total prepaid expenses and other assets	65,742	67,076
Less: Long-term portion	26,668	26,684
Prepaid expenses and other current assets	$39,074	$40,392

8. Accrued expenses and other liabilities

Accrued expenses and other liabilities consisted of the following as of:

(in thousands)	March 31, 2015	December 31, 2014
Taxes payable	$3,174	$4,285
Accrued commissions and salaries	4,915	8,712
Accrued bonuses	8,537	19,480
Lease incentive obligations	4,011	4,099
Deferred rent liabilities	4,244	4,200
Customer credit balances	2,172	2,573
Accrued health care costs	2,440	2,707
Unrecognized tax benefit	3,077	3,791
Other liabilities	10,145	9,791
Total accrued expenses and other liabilities	42,715	59,638
Less: Long-term portion	7,445	7,437
Accrued expenses and other current liabilities	$35,270	$52,201

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9. Deferred revenue

Deferred revenue consisted of the following as of:

(in thousands)	March 31, 2015	December 31, 2014
Subscriptions	$99,467	$98,225
Maintenance	85,915	92,823
Services	28,355	29,457
License fees and other	1,241	769
Total deferred revenue	214,978	221,274
Less: Long-term portion	9,102	8,991
Deferred revenue, current portion	$205,876	$212,283

10. Debt

The following table summarizes our debt balances and the related weighted average effective interest rates, which includes the effect of interest rate swap agreements.

	Debt balance at		Weighted average effective interest rate at	
(in thousands, except percentages)	March 31, 2015	December 31, 2014	March 31, 2015	December 31, 2014
Credit facility:				
Revolving credit loans	$116,900	$110,700	2.09%	1.56%
Term loans	170,625	171,719	2.42%	2.03%
Total debt	287,525	282,419	2.28%	1.85%
Less: Unamortized debt discount	1,737	1,848		
Less: Debt, current portion	4,375	4,375	1.78%	1.39%
Debt, net of current portion	$281,413	$276,196	2.29%	1.85%

We were previously party to a $325.0 million five-year credit facility entered into during February 2012. The credit facility included: a dollar and a designated currency revolving credit facility with sublimits for letters of credit and swingline loans (the “2012 Revolving Facility”) and a delayed draw term loan (the “2012 Term Loan”) together, (the “2012 Credit Facility”).

2014 Refinancing

In February 2014, we entered into a five-year $325.0 million credit facility (the “2014 Credit Facility”) and drew $175.0 million on a term loan upon closing, which was used to repay all amounts outstanding under the 2012 Credit Facility. The 2014 Credit Facility includes the following facilities: (i) a dollar and a designated currency revolving credit facility with sublimits for letters of credit and swingline loans (the “2014 Revolving Facility”) and (ii) a term loan facility (the “2014 Term Loan”).

Certain participants of the 2012 Term Loan participated in the 2014 Term Loan and the change in the present value of our future cash flows to these participants under the 2012 Term Loan and under the 2014 Term Loan was less than 10%. Accordingly, we accounted for the refinancing event for these participants as a debt modification. Certain participants of the 2012 Term Loan did not participate in the 2014 Term Loan. Accordingly, we accounted for the refinancing event for these participants as a debt extinguishment. Certain participants of the 2012 Revolving Facility participated in the 2014 Revolving Facility and provided increased borrowing capacities. Accordingly, we accounted for the refinancing event for these participants as a debt modification. Certain participants of the 2012 Revolving Facility did not participate in the 2014 Revolving Facility. Accordingly, we accounted for the refinancing event for these participants as a debt extinguishment.

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We recorded a $0.4 million loss on debt extinguishment related to the write-off of deferred financing costs for the portions of the 2012 Credit Facility considered to be extinguished. This loss was recognized in the consolidated statements of comprehensive income within loss on debt extinguishment and termination of derivative instruments.
In connection with our entry into the 2014 Credit Facility, we paid $2.5 million in financing costs, of which $1.1 million were capitalized and, together with a portion of the unamortized deferred financing costs from the 2012 Credit Facility and prior facilities, are being amortized into interest expense over the term of the new facility using the effective interest method. As of March 31, 2015 and December 31, 2014, deferred financing costs totaling $1.6 million and $1.7 million, respectively, were included in other assets on the consolidated balance sheet.

Summary of the 2014 Credit Facility

The 2014 Credit Facility is secured by the stock and limited liability company interests of certain of our subsidiaries and is guaranteed by our material domestic subsidiaries.
Amounts borrowed under the dollar tranche revolving credit loans and term loan under the 2014 Credit Facility bear interest at a rate per annum equal to, at our option, (a) a base rate equal to the highest of (i) the prime rate, (ii) federal funds rate plus 0.50% and (iii) one month LIBOR plus 1.00% (the “Base Rate”), in addition to a margin of 0.00% to 0.50%, or (b) LIBOR rate plus a margin of 1.00% to 1.50%. Swingline loans bear interest at a rate per annum equal to the Base Rate plus a margin of 0.00% to 0.50% or such other rate agreed to between the Swingline lender and us. Designated currency tranche revolving credit loans bear interest at a rate per annum equal to the LIBOR rate for the applicable currency plus a margin of 1.00% to 1.50%. The exact amount of any margin depends on the nature of the loan (Base Rate or LIBOR) and our net leverage ratio (as defined in the 2014 Credit Facility).
We also pay a quarterly commitment fee on the unused portion of the 2014 Revolving Facility from 0.15% to 0.225% per annum, depending on our net leverage ratio. At March 31, 2015, the commitment fee was 0.225%.
The term loan under the 2014 Credit Facility requires periodic principal payments. The balance of the term loan and any amounts drawn on the revolving credit loans are due upon maturity of the 2014 Credit Facility in February 2019. We evaluate the classification of our debt as current or non-current based on the required annual maturities of the 2014 Credit Facility.
The 2014 Credit Facility includes financial covenants related to the net leverage ratio and interest coverage ratio, as well as restrictions on our ability to declare and pay dividends and our ability to repurchase shares of our common stock. At March 31, 2015, we were in compliance with our debt covenants under the 2014 Credit Facility.

Financing for MicroEdge Acquisition

The 2014 Credit Facility includes an option to request increases in the revolving commitments and/or request additional term loans in a principal amount of up to $200 million. On October 1, 2014, we exercised this option, and certain lenders agreed, to increase the revolving credit commitments by $100 million such that currently and for the period commencing October 1, 2014, the aggregate revolving credit commitments are $250 million. The additional revolving credit commitments have the same terms as the existing revolving credit commitments.
On October 1, 2014, we drew down $140 million in revolving credit commitments under the 2014 Credit Facility to finance the acquisition of MicroEdge.

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As of March 31, 2015, the required annual maturities related to the 2014 Credit Facility were as follows:

Year ending December 31, (in thousands)	Annual maturities
2015 - remaining	$3,281
2016	4,375
2017	4,375
2018	4,375
2019	271,119
Thereafter	—
Total required maturities	$287,525

11. Derivative instruments

We use derivative instruments to manage interest rate risk. In February 2014, in connection with the refinancing of our debt, we terminated the two interest rate swap agreements associated with the 2012 Credit Facility. As part of the settlement of our swap liabilities, we recorded a loss of $0.6 million, which was recognized in the consolidated statements of comprehensive income within loss on debt extinguishment and termination of derivative instruments. This loss resulted in the recognition of an insignificant tax benefit.

In March 2014, we entered into a new interest rate swap agreement (the "March 2014 Swap Agreement"), which effectively converts portions of our variable rate debt under the 2014 Credit Facility to a fixed rate for the term of the swap agreement. The initial notional value of the March 2014 Swap Agreement was $125.0 million with an effective date beginning in March 2014. In March 2017, the notional value of the March 2014 Swap Agreement will decrease to $75.0 million for the remaining term through February 2018. We designated the March 2014 Swap Agreement as a cash flow hedge at the inception of the contract.

In October 2014, we entered into an additional interest rate swap agreement (the “October 2014 Swap Agreement”), which effectively converts portions of our variable rate debt under the 2014 Credit Facility to a fixed rate for the term of the swap agreement. The initial notional value of the October 2014 Swap Agreement was $75.0 million with an effective date beginning in October 2014. In September 2015, the notional value of the October 2014 Swap Agreement will decrease to $50.0 million for the remaining term through June 2016. We designated the October 2014 Swap Agreement as a cash flow hedge at the inception of the contract.

The fair values of our derivative instruments were as follows as of:

(in thousands)	Balance sheet location	March 31, 2015	December 31, 2014
Derivative instruments designated as hedging instruments:			
Interest rate swaps, long-term portion	Other liabilities	$1,030	$268
Total derivative instruments designated as hedging instruments		$1,030	$268

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Blackbaud, Inc.
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The effects of derivative instruments in cash flow hedging relationships were as follows:

(in thousands)	Gain (loss) recognized in accumulated other comprehensive loss as of March 31, 2015	Location of loss reclassified from accumulated other comprehensive loss into income	Gain (loss) reclassified from accumulated other comprehensive loss into income Three months ended March 31, 2015
Interest rate swaps	$(1,030)	Interest expense	$(375)
	March 31, 2014		Three months ended March 31, 2014
Interest rate swaps	$93	Interest expense	$(214)
Interest rate swaps	—	Loss on debt extinguishment and termination of derivative instruments	(587)
Total	$93		$(801)

Our policy requires that derivatives used for hedging purposes be designated and effective as a hedge of the identified risk exposure at the inception of the contract. Accumulated other comprehensive income (loss) includes unrealized gains or losses from the change in fair value measurement of our derivative instruments each reporting period and the related income tax expense or benefit. Changes in the fair value measurements of the derivative instruments and the related income tax expense or benefit are reflected as adjustments to accumulated other comprehensive income (loss) until the actual hedged expense is incurred or until the hedge is terminated at which point the unrealized gain (loss) is reclassified from accumulated other comprehensive income (loss) to current earnings. There were no ineffective portions of our interest rate swap derivatives during the three months ended March 31, 2015 and 2014. See Note 15 to these consolidated financial statements for a summary of the changes in accumulated other comprehensive income (loss) by component.

12. Commitments and contingencies

Leases

We lease our headquarters facility under a 15-year lease agreement which was entered into in October 2008, and has two five-year renewal options. The current annual base rent of the lease is $4.1 million, payable in equal monthly installments. The base rent escalates annually at a rate equal to the change in the consumer price index, as defined in the agreement, but not to exceed 5.5% in any year.

We have a lease for office space in Austin, Texas which terminates on September 30, 2023, and has two five-year renewal options. Under the terms of the lease, we will increase our leased space by approximately 20,000 square feet on July 31, 2016. The current annual base rent of the lease is $2.3 million. The base rent escalates annually between 2% and 4% based on the terms of the agreement. The rent expense is recorded on a straight-line basis over the length of the lease term. At March 31, 2015, we had a standby letter of credit of $2.0 million for a security deposit for this lease.

We have provisions in our leases that entitle us to aggregate remaining leasehold improvement allowances of $5.5 million. These amounts are being recorded as a reduction to rent expense ratably over the terms of the leases. The

reductions in rent expense related to these lease provisions during the three months ended March 31, 2015 and 2014, were insignificant. The leasehold improvement allowances have been included in the table of operating lease commitments below as a reduction in our lease commitments ratably over the then remaining terms of the leases. The timing of the reimbursements for the actual leasehold improvements may vary from the amounts reflected in the table below.

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We have also received, and expect to receive through 2016, quarterly South Carolina state incentive payments as a result of locating our headquarters facility in Berkeley County, South Carolina. These amounts are recorded as a reduction of rent expense upon receipt and were $0.6 million and $0.5 million for the three months ended March 31, 2015 and 2014, respectively.

Total rent expense was $2.5 million and $2.2 million for the three months ended March 31, 2015 and 2014, respectively.

As of March 31, 2015, the future minimum lease commitments related to lease agreements, net of related lease incentives, were as follows:

Year ending December 31, (in thousands)	Operating leases
2015 – remaining	$9,156
2016	11,647
2017	10,844
2018	11,109
2019	10,460
Thereafter	33,774
Total minimum lease payments	$86,990

Other commitments

As discussed in Note 10 to these consolidated financial statements, the term loans under the 2014 Credit Facility require periodic principal payments. The balance of the term loans and any amounts drawn on the revolving credit loans are due upon maturity of the 2014 Credit Facility in February 2019.

We utilize third-party technology in conjunction with our products and services, with contractual arrangements varying in length from one to five years. In certain cases, these arrangements require a minimum annual purchase commitment. As of March 31, 2015, the remaining aggregate minimum purchase commitment under these arrangements was approximately $14.5 million through 2018. We incurred expense under these arrangements of $2.1 million for the three months ended March 31, 2015.

Legal contingencies

We are subject to legal proceedings and claims that arise in the ordinary course of business. We record an accrual for a contingency when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. We do not believe the amount of potential liability with respect to these actions will have a material adverse effect upon our consolidated financial position, results of operations or cash flows.

13. Income taxes

Our effective income tax rates including the effects of period-specific events, were:

	Three months ended March 31,	
	2015	2014
Effective tax rate	29.0%	42.2%

The decrease in our effective income tax rate during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily due to a discrete tax benefit from the settlement of an Internal Revenue Service ("IRS") audit.

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Our effective income tax rate may fluctuate quarterly as a result of factors, including transactions entered into, changes in the geographic distribution of our earnings or losses, our assessment of certain tax contingencies, valuation allowances, and changes in tax law in jurisdictions where we conduct business.

We have deferred tax assets for federal, state, and international net operating loss carryforwards and state tax credits. The federal and state net operating loss carryforwards are subject to various Internal Revenue Code limitations and applicable state tax laws. A portion of the foreign and state net operating loss carryforwards and a portion of state tax credits have a valuation reserve due to the uncertainty of realizing such carryforwards and credits in the future.

The total amount of unrecognized tax benefit that, if recognized, would favorably affect the effective income tax rate, was $2.3 million and $2.8 million at March 31, 2015 and December 31, 2014, respectively. We recognize accrued interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense.

14. Stock-based compensation

Stock-based compensation expense is allocated to cost of revenue and operating expenses on the consolidated statements of comprehensive income based on where the associated employee’s compensation is recorded. The following table summarizes stock-based compensation expense:

	Three months ended March 31,	
(in thousands)	2015	2014
Included in cost of revenue:		
Cost of subscriptions	$143	$189
Cost of maintenance	161	145
Cost of services	597	542
Total included in cost of revenue	901	876
Included in operating expenses:		
Sales and marketing	701	471
Research and development	978	662
General and administrative	2,522	1,705
Total included in operating expenses	4,201	2,838
Total stock-based compensation expense	$5,102	$3,714

15. Stockholders' equity

Dividends

In February 2015, our Board of Directors approved an annual dividend rate of $0.48 per share to be made in quarterly payments. Dividend payments are not guaranteed and our Board of Directors may decide, in its absolute discretion, at any time and for any reason, not to declare or pay further dividends. The following table provides information with respect to quarterly dividends of $0.12 per share paid on common stock during the three months ended March 31, 2015.

Declaration Date	Dividend per Share	Record Date	Payable Date
February 2015	$0.12	February 27	March 13

In April 2015, our Board of Directors declared a second quarter dividend of $0.12 per share payable on June 15, 2015 to stockholders of record on May 28, 2015.

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Changes in accumulated other comprehensive loss by component

The changes in accumulated other comprehensive loss by component, consisted of the following:

	Three months ended March 31,	
(in thousands)	2015	2014
Accumulated other comprehensive loss, beginning of period	$(1,032)	$(1,385)
By component:		
Gains and losses on cash flow hedges:		
Accumulated other comprehensive loss balance, beginning of period	$(164)	$(256)
Other comprehensive loss before reclassifications, net of tax effects of $439 and $113	(698)	(169)
Amounts reclassified from accumulated other comprehensive loss to interest expense	375	214
Amounts reclassified from accumulated other comprehensive loss to loss on debt extinguishment and termination of derivative instruments	—	587
Tax benefit included in provision for income taxes	(146)	(320)
Total amounts reclassified from accumulated other comprehensive loss	229	481
Net current-period other comprehensive (loss) income	(469)	312
Accumulated other comprehensive (loss) income balance, end of period	$(633)	$56
Foreign currency translation adjustment:		
Accumulated other comprehensive loss balance, beginning of period	$(868)	$(1,129)
Translation adjustments	(326)	555
Accumulated other comprehensive loss balance, end of period	(1,194)	(574)
Accumulated other comprehensive loss, end of period	$(1,827)	$(518)

16. Segment information

In March 2015, we implemented a new internal reporting structure in which Target Analytics is no longer being viewed as a stand-alone business unit, but rather as a suite of solutions being sold by the Enterprise Customer Business Unit (the “ECBU”), the General Markets Business Unit (the “GMBU”), and the International Business Unit (the “IBU”). As a result of the change in our internal reporting structure, which was effective beginning in March 2015, the operating results of Target Analytics are no longer regularly reviewed by our chief operating decision maker ("CODM") to make decisions about resources to be allocated and to assess performance, and therefore, Target Analytics no longer meets the definition of an operating segment. In addition, Target Analytics did not meet any of the quantitative thresholds set forth in ASC 280, Segment Reporting, during the three months ended March 31, 2014 and had been previously disclosed for informational purposes. The change in reportable segments had no effect on our consolidated financial position, results of operations or cash flows for the periods presented.

As of March 31, 2015, our reportable segments were the ECBU, the GMBU, and the IBU. Following is a description of each reportable segment:

- The ECBU is focused on marketing, sales, delivery and support to all large and/or strategic prospects and customers in North America;
- The GMBU is focused on marketing, sales, delivery and support to all emerging and mid-sized prospects and customers in North America; and
- The IBU is focused on marketing, sales, delivery and support to all prospects and customers outside of North America.

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(Unaudited)

Our CODM is our chief executive officer, or CEO. The CEO reviews financial information presented on an operating segment basis for the purposes of making certain operating decisions and assessing financial performance. The CEO uses internal financial reports that provide segment revenues and operating income, excluding stock-based compensation expense, amortization expense, depreciation expense, research and development expense and certain corporate sales, marketing, general and administrative expenses. Currently, the CEO believes that the exclusion of these costs allows for a better understanding of the operating performance of the operating units and management of other operating expenses and cash needs. The CEO does not review any segment balance sheet information.
We have recast our segment disclosures for the three months ended March 31, 2014 in order to present them on a consistent basis with our change in reportable segments in the current year. Summarized reportable segment financial results, were as follows:

	Three months ended March 31,	
(in thousands)	2015	2014
Revenue by segment:		
ECBU	$66,914	$55,825
GMBU	69,929	61,130
IBU	10,127	10,642
Other[1]	23	25
Total revenue	$146,993	$127,622
Segment operating income[2]:		
ECBU	$32,204	$27,027
GMBU	34,663	32,745
IBU	1,301	1,050
Other[1]	(312)	232
	67,856	61,054
Less:		
Corporate unallocated costs[3]	46,615	42,039
Stock based compensation costs	5,102	3,714
Amortization expense	8,127	6,024
Interest expense, net	1,678	1,443
Loss on debt extinguishment and termination of derivative instruments	—	996
Other expense, net	295	236
Income before provision for income taxes	$6,039	$6,602

(1) Other includes revenue and the related costs from the sale of products and services not directly attributable to an operating segment.

(2) Segment operating income includes direct, controllable costs related to the sale of products and services by the reportable segment.

(3) Corporate unallocated costs include research and development, depreciation expense, and certain corporate sales, marketing, general and administrative expenses.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q. This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements reflect our current view with respect to future events and financial performance and are subject to risks and uncertainties, including those set forth under “Cautionary Statement Regarding Forward-Looking Statements” at the beginning of this report and elsewhere in this report, that could cause actual results to differ materially from historical or anticipated results. Except as required by law, we do not intend, and undertake no obligation to revise or update these forward-looking statements, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

Executive summary

We provide software and services for the nonprofit, charitable giving and education communities. Our offerings include a full spectrum of cloud-based and on-premise solutions, and related services for organizations of all sizes, including nonprofit fundraising and relationship management, marketing, advocacy, accounting, payments and analytics, as well as grant management, corporate social responsibility, education and other solutions. We continue to make investments in our product portfolio and go-to-market organization to ensure we are well positioned to benefit from shifts in the market, including demand for our cloud-based subscription offerings. As of March 31, 2015, we had more than 30,000 active customers including nonprofits, K12 private and higher education institutions, healthcare organizations, foundations and other charitable giving entities, and corporations.

During the first quarter of 2015, we continued to execute on the following five growth and operational improvement strategies targeted to drive an extended period of quality enhancement, product and service innovation, and increasing operating efficiency and financial performance:

1. Accelerate organic revenue growth;
2. Accelerate our product portfolio's move to the cloud;
3. Expand our total addressable market;
4. Optimize our back-office infrastructure; and
5. Implement a margin improvement plan.

We completed our acquisitions of WhippleHill and MicroEdge in June 2014 and October 2014, respectively. We have included the results of operations of acquired companies in our consolidated results of operations from the date of their respective acquisition, which impacts the comparability of our results of operations when comparing the three months ended March 31, 2015 and 2014. We have noted in the discussion below, to the extent meaningful, the impact on the comparability of our consolidated results of operations to prior year results due to the inclusion of acquired companies.

We derive revenue from charging subscription fees for the use of our cloud-based solutions, selling perpetual licenses and providing a broad offering of services, including consulting, training, installation and implementation services, as well as ongoing customer support and maintenance. Furthermore, we derive revenue from providing hosting services, performing donor prospect research engagements, selling lists of potential donors, providing transaction and payment processing services, benchmarking studies and data modeling services. We have experienced growth in our payment processing services from the continued shift to online giving, further integration of these services to our existing product portfolio and the sale of these services to new and existing customers.

Total revenue for the three months ended March 31, 2015 increased by approximately 15% when compared to the same period in 2014. The inclusion of MicroEdge added $6.6 million of incremental revenue and WhippleHill also positively impacted revenue for the three months ended March 31, 2015 when compared to the same period in 2014. Excluding the impact of these acquisitions, our revenue growth was primarily driven by growth in subscriptions revenue. During the three months ended March 31, 2015, we experienced an increase in demand for our cloud-based

and hosted solutions as our business continues to shift towards providing predominantly subscription-based offerings. Subscriptions revenue also grew as a result of increases in the number of customers and volume of transactions for which we process payments, and an increase in usage-based transaction revenue.

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Income from operations for the three months ended March 31, 2015 decreased by $1.3 million when compared to the same period in 2014. The decrease in income from operations was primarily attributable to a $2.1 million increase in amortization of intangible assets from business combinations, an increase in stock-based compensation and charges recorded for employee severance. These unfavorable impacts on income from operations were partially offset by the increase subscription revenue discussed above as well as the incremental investments we made during the three months ended March 31, 2014 that were targeted to drive the success of our five growth and operational improvement strategies, which did not recur in the three months ended March 31, 2015.

At March 31, 2015, our cash and cash equivalents were $13.3 million and outstanding borrowings under the 2014 Credit Facility were $285.8 million. During the three months ended March 31, 2015, we generated $4.2 million in cash flow from operations, increased net borrowings by $5.1 million, returned $5.6 million to stockholders by way of dividends and had cash outlays of $5.7 million for purchases of property and equipment and software development costs.

We plan to further increase our focus on cloud-based subscription offerings and expand our payment processing and analytics services as we execute on our key growth initiatives and strengthen our market leadership position, while achieving our targeted level of profitability. In the near term, we anticipate that there will continue to be an impact from our payment processing services on our overall gross and operating margins as growth in the volume of transactions where we provide payment processing services is expected to exceed the growth of certain other product and service offerings.

We also plan to continue to invest in our product, sales and marketing organizations and our back-office processes as well as the infrastructure that supports our cloud-based subscription offerings and certain product development initiatives to achieve optimal scalability of our operations as we execute on our key growth initiatives.

Comparison of the three months ended March 31, 2015 and 2014

Results of operations

We have included the results of operations of acquired companies in our consolidated results of operations from the date of their respective acquisition, which impacts the comparability of our results of operations when comparing the three months ended March 31, 2015 and 2014. We have noted in the discussion below, to the extent meaningful, the impact on the comparability of our consolidated results of operations to prior year results due to the inclusion of acquired companies.

We acquired WhippleHill on June 16, 2014. Because we have integrated WhippleHill's operations, it is impracticable to determine the revenue and operating costs attributable solely to the acquired business. We acquired MicroEdge on October 1, 2014. For the three months ended March 31, 2015, MicroEdge's total revenue was $6.6 million. Because we have integrated a substantial portion of MicroEdge's operations, it is impracticable to determine the operating costs attributable solely to the acquired business. See Note 3 to our consolidated financial statements for a summary of these acquisitions.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Revenue by segment

	Three months ended March 31,			
(in millions, except percentages)	2015	2014	Change	% Change
ECBU	$66.9 [1]	$55.8	$11.1	20 %
GMBU	69.9	61.1	8.8	14 %
IBU	10.1	10.6	(0.5)	(5)%
Other	—	—	—	100 %
Total revenue[2]	$147.0	$127.6	$19.4	15 %

(1) Included in ECBU revenue for the three months ended March 31, 2015 was $6.6 million attributable to the inclusion of MicroEdge.
(2) The individual amounts for each year may not sum to total revenue due to rounding.

When removing the impact attributable to MicroEdge as discussed above, the increase in ECBU revenue during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily attributable to growth in subscriptions revenue. The growth in subscriptions resulted primarily from increases in demand for our hosted solution Blackbaud CRM and our cloud-based solution Luminate CRM. ECBU subscriptions revenue also benefited from increases in the number of customers and the volume of transactions for which we process payments, and an increase in usage-based transaction revenue. Also contributing to the overall growth in ECBU revenue was an increase in consulting services revenue related to our Blackbaud CRM and Luminate Online solutions and maintenance revenue primarily from new Blackbaud CRM customers.

The increase in GMBU revenue during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily attributable to growth in subscriptions revenue and the contribution of revenue from WhippleHill. The growth in subscriptions revenue was primarily due to strong demand for our hosted solutions including the Raiser's Edge and Financial Edge as well as our cloud-based solutions including Altru and Online Express. GMBU subscriptions revenue also benefited from increases in the number of customers and the volume of transactions for which we process payments, and an increase in usage-based transaction revenue. Also contributing to overall growth in GMBU revenue was an increase in consulting services revenue related to our Luminate Online and Raiser's Edge solutions.

The decrease in IBU revenue during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily related to a reduction in perpetual license sales of our Raiser's Edge solution. Also contributing to the decrease in IBU revenue was a decrease in consulting services revenue related to our Raiser's Edge solution.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Operating results
Subscriptions

	Three months ended March 31,			
(in millions, except percentages)	2015	2014	Change	% Change
Subscriptions revenue	$72.5 (1)	$58.3	$14.2	24 %
Cost of subscriptions	36.2	30.1	6.1	20 %
Subscriptions gross profit	$36.3	$28.2	$8.1	29 %
Subscriptions gross margin	50 %	48 %		

(1) Included in subscriptions revenue for the three months ended March 31, 2015 was $3.7 million attributable to the inclusion of MicroEdge.

Subscriptions revenue is comprised of revenue from charging for the use of our subscription-based software products, which includes providing access to hosted applications and hosting services, access to certain data services and our online subscription training offerings, revenue from payment processing services as well as variable transaction revenue associated with the use of our products. We continue to experience growth in sales of our hosted applications and hosting services as we meet the demand of our customers that increasingly prefer cloud-based subscription offerings. In addition, we have experienced growth in our payment processing services from the continued shift to online giving, further integration of these services to our existing product portfolio and the sale of these services to new and existing customers.

Excluding the incremental subscriptions revenue from MicroEdge as discussed above, the increase in subscriptions revenue during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily due to strong demand for our cloud-based solutions including Luminate CRM and Altru and for our hosted solutions including Blackbaud CRM, the Raiser's Edge and the Financial Edge. Subscriptions revenue also grew as a result of increases in the number of customers and the volume of transactions for which we process payments, and an increase in usage-based transaction revenue. Also contributing to the increase in subscriptions revenue was the inclusion of WhippleHill during the three months ended March 31, 2015.

Cost of subscriptions is primarily comprised of human resource costs, stock-based compensation expense, third-party royalty and data expenses, hosting expenses, allocated depreciation, facilities and IT support costs, amortization of intangibles from business combinations, transaction-based costs related to payments services, remittances of amounts due to third-parties under our payment processing services and other costs incurred in providing support and services to our customers.

The increase in cost of subscriptions during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily due to an increase in transaction-based costs related to our payments services of $1.7 million, an increase in human resource costs of $1.5 million and an increase in amortization of intangible assets from business combinations of $1.2 million. The increase in human resource costs was primarily due to an increase in subscription customer support headcount directly related to our growing base of subscription customers. The inclusion of WhippleHill and MicroEdge also contributed to the increase in human resource costs.

The increase in subscriptions gross margin for the three months ended March 31, 2015, when compared to the same period in 2014, was primarily due to the increase in subscriptions revenue outpacing the growth in transaction-based costs related to our payments services and human resource costs, as we achieved economies of scale. In the near term, we anticipate that there will continue to be a negative impact from our payment processing services on our subscriptions gross margin percentage as growth in the volume of transactions where we provide payment processing services is expected to exceed the growth of certain of our other cloud-based subscription offerings.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Maintenance

	Three months ended March 31,				
(in millions, except percentages)	2015	2014	Change	% Change	
Maintenance revenue	$38.9 (1)	$35.7	$3.2	9	%
Cost of maintenance	7.5	5.4	2.1	39	%
Maintenance gross profit	$31.4	$30.3	$1.1	4	%
Maintenance gross margin	81 %	85 %			

(1) Included in maintenance revenue for the three months ended March 31, 2015 was $2.4 million attributable to the inclusion of MicroEdge.

Maintenance revenue is comprised of annual fees derived from maintenance contracts associated with new software licenses and annual renewals of existing maintenance contracts. These contracts provide customers with updates, enhancements and upgrades to our software products and online, telephone and email support. Maintenance contracts are typically for a term of one year, and maintenance renewal rates in the period reported did not vary materially compared to prior periods. Over time, we anticipate a decrease in maintenance contract renewals as we transition our product portfolio to a cloud-based subscription delivery model and away from a perpetual license-based model.

Excluding the incremental maintenance revenue from MicroEdge as discussed above, the increase in maintenance revenue during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily comprised of (i) $2.6 million of incremental maintenance from new customers associated with new license agreements and increases in contracts with existing customers; and (ii) approximately $0.9 million of incremental maintenance from contractual inflationary rate adjustments; partially offset by (iii) a $2.6 million reduction in maintenance from contracts that were not renewed and reductions in contracts with existing customers.

Cost of maintenance is primarily comprised of human resource costs, stock-based compensation expense, third-party contractor expenses, third-party royalty costs, allocated depreciation, facilities and IT support costs, amortization of intangibles from business combinations and other costs incurred in providing support and services to our customers.

Cost of maintenance increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily as a result of an increase in amortization of intangible assets from business combinations of $1.0 million and an increase in human resource costs of $0.5 million, primarily due to the inclusion of MicroEdge. Partially offsetting this increase in human resource costs was a reduction in customer support costs as our business shifts towards cloud-based subscriptions, which is a trend that is likely to continue.

Maintenance gross margin decreased during the three months ended March 31, 2015 when compared to the same period in 2014, primarily due to the incremental amortization of intangible assets from business combinations and human resource costs attributable to MicroEdge.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Services

	Three months ended March 31,				
(in millions, except percentages)	2015	2014	Change	% Change	
Services revenue	$31.3	$28.1	$3.2	11	%
Cost of services	27.0	26.3	0.7	3	%
Services gross profit	$4.3	$1.8	$2.5	139	%
Services gross margin	14	%6	%		

We derive services revenue from consulting, implementation, education, analytic and installation services. Consulting, implementation and installation services involve converting data from a customer’s existing system, system configuration, process re-engineering and assistance in file set up. Education services involve customer training activities. Analytic services are comprised of donor prospect research, sales of lists of potential donors, benchmarking studies and data modeling services. These analytic services involve the assessment of current and prospective donor information of the customer and are performed using our proprietary analytical tools. The end product is intended to enable organizations to more effectively target their fundraising activities.

Services revenue increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily as a result of an increase in consulting services revenue of $2.9 million related to our Blackbaud CRM and Luminate Online solutions. We expect that the continuing shift in our go-to-market strategy towards cloud-based subscription offerings, which, in general, require less implementation services and little to no customization services when compared our traditional on-premise perpetual license arrangements, will negatively impact consulting services revenue growth.

Cost of services is primarily comprised of human resource costs, stock-based compensation expense, third-party contractor expenses, classroom rentals, costs incurred in providing customer training, data expense incurred to perform analytic services, allocated depreciation, facilities and IT support costs and amortization of intangibles from business combinations. Cost of services during the three months ended March 31, 2015, when compared to the same period in 2014, was relatively unchanged.

Services gross margin increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to the increase in consulting services revenue relative to the modest change in cost of services.

License fees and other

	Three months ended March 31,				
(in millions, except percentages)	2015	2014	Change	% Change	
License fees and other revenue	$4.3	$5.6	$(1.3	) (23	)%
Cost of license fees and other	1.2	1.5	(0.3	) (20	)%
License fees and other gross profit	$3.1	$4.1	$(1.0	) (24	)%
License fees and other gross margin	72	%73	%		

License fees and other revenue includes revenue from the sale of our software products under perpetual license agreements, the sale of business forms that are used in conjunction with our software products, reimbursement of travel-related expenses primarily incurred during the performance of services at customer locations, fees from user conferences and third-party software referral fees.

During the three months ended March 31, 2015, revenue from license fees and other decreased primarily as a result of a continued shift in our customers’ buying preferences away from software offered under perpetual license arrangements towards cloud-based subscription offerings.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Cost of license fees and other is primarily comprised of third-party software royalties, variable reseller commissions, amortization of software development costs, human resource costs, costs of business forms, costs of user conferences, reimbursable expenses relating to the performance of services at customer locations, allocated depreciation, facilities and IT support costs and amortization of intangibles from business combinations.

The decrease in cost of license fees and other during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily due to less reimbursable expenses related to services provided at customer locations and a reduction in reseller commissions.

License fees and other gross margin decreased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to the shift in our customers' buying preferences towards cloud-based subscription offerings relative to the modest decrease in cost of license fees and other.

Operating expenses

Sales and marketing

	Three months ended March 31,				
(in millions, except percentages)	2015	2014	Change	% Change	
Sales and marketing expense	$28.6	$25.1	$3.5	14	%
% of revenue	19 %	20 %			

Sales and marketing expense includes human resource costs, stock-based compensation expense, travel-related expenses, sales commissions, advertising and marketing materials, public relations costs and allocated depreciation, facilities and IT support costs.

Sales and marketing expense increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to increases in human resource costs, advertising and marketing materials and commission expense of $1.4 million, $0.5 million and $0.5 million, respectively. Human resource costs increased primarily due to incremental headcount to support the increase in sales and marketing efforts of our growing operations. The inclusion of WhippleHill and MicroEdge also contributed to the increases in human resource costs. Advertising and marketing materials increased as a result of the inclusion of WhippleHill and MicroEdge. The increase in commission expense was primarily driven by an increase in commissionable revenue during the three months ended March 31, 2015, when compared to the same period in 2014.

Sales and marketing expense as a percentage of revenue remained relatively unchanged during the three months ended March 31, 2015, when compared to the same period in 2014.

Research and development

	Three months ended March 31,				
(in millions, except percentages)	2015	2014	Change	% Change	
Research and development expense	$21.3	$16.5	$4.8	29	%
% of revenue	14 %	13 %			

Research and development expense includes human resource costs, stock-based compensation expense, third-party contractor expenses, software development tools and other expenses related to developing new products, upgrading and enhancing existing products, and allocated depreciation, facilities and IT support costs.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Research and development expense increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to increases in human resource costs and allocated depreciation, facilities and IT support costs of $4.9 million and $0.8 million, respectively. Partially offsetting these increases was a $2.0 million increase in the amount of software development costs that were capitalized from an increase in development activities that generate costs which qualify for capitalization as internal-use software. The inclusion of WhippleHill and MicroEdge also contributed to the increases in human resource costs and allocated costs.

Research and development expense as a percentage of revenue increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to the inclusion of WhippleHill and MicroEdge.

General and administrative

	Three months ended March 31,			
(in millions, except percentages)	2015	2014	Change	% Change
General and administrative expense	$16.8	$12.8	$4.0	31 %
% of revenue	11 %	10 %		

General and administrative expense consists primarily of human resource costs for general corporate functions, including senior management, finance, accounting, legal, human resources and corporate development, stock-based compensation expense, third-party professional fees, insurance, allocated depreciation, facilities and IT support costs, acquisition-related expense and other administrative expenses.

General and administrative expense increased during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to increases in human resource and facilities costs, stock-based compensation expense and acquisition-related expenses of $4.3 million, $0.8 million and $0.6 million, respectively. Partially offsetting these increases was a decrease in other corporate costs of $1.8 million. Human resource costs increased primarily due to additional resources needed to support the growth of our business and the inclusion of WhippleHill and MicroEdge. The increase in facilities and acquisition-related expenses was due to our acquisitions of WhippleHill and MicroEdge. The increase in stock-based compensation expense was primarily attributable to a change in timing of equity award grants and certain senior management hires, including our CEO.

General and administrative expense increased as a percentage of revenue during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to the inclusion of WhippleHill and MicroEdge.

Non-GAAP financial measures

The operating results analyzed below are presented on a non-GAAP basis. We use non-GAAP revenue, non-GAAP income from operations, non-GAAP operating margin, EBITDA and Adjusted EBITDA internally in analyzing our operational performance. Accordingly, we believe these non-GAAP measures are useful to investors, as a supplement to GAAP measures, in evaluating our ongoing operational performance. While we believe these non-GAAP measures provide useful supplemental information, non-GAAP financial measures should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with GAAP. In addition, these non-GAAP financial measures may not be completely comparable to similarly titled measures of other companies due to potential differences in the exact method of calculation between companies.

We have acquired businesses whose net tangible assets include deferred revenue. In accordance with GAAP reporting requirements, we recorded write-downs of deferred revenue to fair value, which resulted in lower recognized revenue for a certain period of time until the related obligations to provide services are fulfilled. Therefore, our GAAP revenues after the acquisitions will not reflect the full amount of revenue that would have been reported if the acquired

deferred revenue was not written down to fair value. The non-GAAP measures described below reverse the acquisition-related deferred revenue write-downs so that the full amount of revenue booked by the acquired companies is included, which we believe provides a more accurate representation of a revenue run-rate in a given period.

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Blackbaud, Inc.
Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

The non-GAAP financial measures discussed below exclude the impact of certain transactions because we believe they are not directly related to our operating performance in any particular period, but are for our long-term benefit over multiple periods. We believe that these non-GAAP financial measures reflect our ongoing business in a manner that allows for meaningful period-to-period comparisons and analysis of trends in our business.

	Three months ended March 31,				
(in millions, except percentages)	2015	2014	Change	% Change	
GAAP Revenue	$147.0	$127.6	$19.4	15	%
Non-GAAP adjustments:					
Add: Acquisition-related deferred revenue write-down	3.5	—	3.5	100	%
Non-GAAP revenue	$150.5	$127.6	$22.9	18	%
GAAP income from operations	$8.0	$9.3	$(1.3)	(14)	%
GAAP operating margin	5.5%	7.3%			
Non-GAAP adjustments:					
Add: Acquisition-related deferred revenue write-down	3.5	—	3.5	100	%
Add: Stock-based compensation expense	5.1	3.7	1.4	38	%
Add: Amortization of intangibles from business combinations	8.1	6.0	2.1	35	%
Add: Employee severance	1.1	—	1.1	100	%
Add: Acquisition-related integration costs	0.5	—	0.5	100	%
Add: Acquisition-related expenses	0.1	—	0.1	100	%
Add: CEO transition costs	—	0.9	(0.9)	(100)	%
Subtotal[(1)]	18.4	10.6	7.8	74	%
Non-GAAP income from operations[(1)]	$26.5	$19.9	$6.6	33	%
Non-GAAP operating margin	17.6%	15.6%			

(1) The individual amounts for each year may not sum to subtotal or Non-GAAP income from operations due to rounding.

The increases in non-GAAP income from operations and non-GAAP operating margin during the three months ended March 31, 2015, when compared to the same period in 2014, were primarily due to the strong growth in subscriptions revenue and the incremental revenue from acquired companies as discussed above, partially offset by increases in human resource costs, transaction-based costs related to payments services and hosting costs. Also contributing to the increases in non-GAAP income from operations and non-GAAP operating margin were the incremental investments we made during the three months ended March 31, 2014 that were targeted to drive the success of our five growth and operational improvement strategies, which did not recur in the three months ended March 31, 2015. While we continue to invest in these strategies, the amount of investments has decreased in the three months ended March 31, 2015, when compared to the same period in 2014.

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Blackbaud, Inc.
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(in millions, except percentages)	Three months ended March 31,				
	2015	2014	Change	% Change	
GAAP net income	$4.3	$3.8	0.5	13	%
Non-GAAP adjustments:					
Add: Interest, net	1.7	1.4	0.3	21	%
Add: Income tax provision	1.8	2.8	(1.0)	(36)	%
Add: Depreciation	4.8	4.3	0.5	12	%
Add: Amortization of intangibles from business combinations	8.1	6.0	2.1	35	%
Add: Amortization of software development costs	0.8	0.3	0.5	167	%
Subtotal[(1)]	17.1	14.9	2.2	15	%
EBITDA[(1)]	$21.4	$18.7	$2.7	14	%
EBITDA Margin	14.2 %	14.7 %			
Non-GAAP adjustments:					
Add: Other expense, net	$0.3	$0.2	$0.1	50	%
Add: Loss on debt extinguishment and termination of derivative instruments	—	1.0	(1.0)	(100)	%
Add: Acquisition-related deferred revenue write-down	3.5	—	3.5	100	%
Add: Stock-based compensation expense	5.1	3.7	1.4	38	%
Add: Employee severance	1.1	—	1.1	100	%
Add: Acquisition-related integration costs	0.5	—	0.5	100	%
Add: Acquisition-related expenses	0.1	—	0.1	100	%
Add: CEO transition costs	—	0.9	(0.9)	(100)	%
Subtotal[(1)]	10.6	5.8	4.8	83	%
Adjusted EBITDA[(1)]	$32.0	$24.5	$7.5	31	%
Adjusted EBITDA Margin	21.3 %	19.2 %			

(1) The individual amounts for each year may not sum to subtotals, EBITDA or Adjusted EBITDA due to rounding.

Interest expense

Interest expense during the three months ended March 31, 2015, when compared to the same period in 2014, remained relatively unchanged.

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Blackbaud, Inc.
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Deferred revenue

The table below compares the components of deferred revenue from our consolidated balance sheets:

(in millions)	Timing of recognition	March 31, 2015	December 31, 2014	Change	% Change
Subscriptions	Over the period billed in advance, generally one year	$99.5	$98.2	$1.3	1 %
Maintenance	Over the period billed in advance, generally one year	85.9	92.8	(6.9)	(7)%
Services	As services are delivered	28.4	29.5	(1.1)	(4)%
License fees and other	Upon delivery of the product or service	1.2	0.8	0.4	50 %
Total deferred revenue		215.0	221.3	(6.3)	(3)%
Less: Long-term portion		9.1	9.0	0.1	1 %
Current portion		$205.9	$212.3	$(6.4)	(3)%

(1) The individual amounts for each year may not sum to total deferred revenue due to rounding.

To the extent that our customers are billed for our products and services in advance of delivery, we record such amounts in deferred revenue. Deferred revenue attributable to maintenance decreased during the three months ended March 31, 2015 primarily as a result of a seasonal decrease in billings for maintenance renewals. Historically, due to the timing of client budget cycles, we have less customer contract renewals in our first quarter as compared to our second and fourth quarters. We generally invoice our maintenance and subscription customers in annual cycles 30 days prior to the end of the contract term. The increase in deferred revenue from license fees and other during the three months ended March 31, 2015 was primarily due to a seasonal increase in advance registration billings associated with our K12 user conference, which occurs in July each year. Deferred revenue from subscriptions and services remained relatively unchanged during the three months ended March 31, 2015.

Income tax provision

Our effective income tax rates, including the effects of period-specific events, were:

	Three months ended March 31,	
	2015	2014
Effective tax rate	29.0 %	42.2 %

The decrease in our effective income tax rate during the three months ended March 31, 2015, when compared to the same period in 2014, was primarily due to a discrete tax benefit from the settlement of an IRS audit.

Our effective income tax rate may fluctuate quarterly as a result of factors, including transactions entered into, changes in the geographic distribution of our earnings or losses, our assessment of certain tax contingencies, valuation allowances, and changes in tax law in jurisdictions where we conduct business.

We have deferred tax assets for federal, state, and international net operating loss carryforwards and state tax credits. The federal and state net operating loss carryforwards are subject to various Internal Revenue Code limitations and applicable state tax laws. A portion of the foreign and state net operating loss carryforwards and a portion of state tax credits have a valuation reserve due to the uncertainty of realizing such carryforwards and credits in the future.

The total amount of unrecognized tax benefit that, if recognized, would favorably affect the effective income tax rate, was $2.3 million and $2.8 million at March 31, 2015 and December 31, 2014, respectively. We recognize accrued interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense.

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Seasonality

Our revenues normally fluctuate as a result of certain seasonal variations in our business. Our revenue from professional services has historically been lower in the first quarter when many of those services commence and in the fourth quarter due to the holiday season. In addition, our transaction revenue has historically been at its lowest in the first quarter due to the timing of customer fundraising initiatives and events. As a result of these and other factors, our total revenue has historically been lower in the first quarter than in the remainder of our fiscal year, with the third and fourth quarters historically achieving the highest total revenues. Our revenue from payment processing services has also historically increased during the fourth quarter due to year-end giving. Our expenses, however, do not vary significantly as a result of these factors, but do fluctuate on a quarterly basis due to varying timing of expenditures. Our cash flow from operations normally fluctuates quarterly due to the combination of the timing of customer contract renewals, delivery of professional services and occurrence of customer events as well as the payment of bonuses, among other factors. Historically, due to lower revenues in our first quarter, combined with the payment of bonuses from the prior year in our first quarter, our cash flow from operations has been lowest in our first quarter, and due to the timing of client budget cycles, our cash flow from operations has been lower in our second quarter as compared to our third and fourth quarters. In addition, deferred revenues can vary on a seasonal basis for the same reasons. These patterns may change, however, as a result of the continued shift to online giving, growth in volume of transactions for which we process payments, acquisitions, new market opportunities, new product introductions or other factors.

Liquidity and capital resources

At March 31, 2015, cash and cash equivalents totaled $13.3 million, compared to $14.7 million at December 31, 2014. The $1.4 million decrease in cash and cash equivalents during the three months ended March 31, 2015, was principally attributable to the payment of dividends of $5.6 million and cash outlays for purchases of property and equipment and software development costs totaling $5.7 million, partially offset by cash generated from operations of $4.2 million and a net increase in borrowings of $5.1 million.

Our principal sources of liquidity are operating cash flow, funds available under the 2014 Credit Facility and cash on hand. Our operating cash flow depends on continued customer renewal of our subscription, maintenance and support agreements and market acceptance of our products and services. Based on current estimates of revenue and expenses, we believe that the currently available sources of funds and anticipated cash flows from operations will be adequate for at least the next twelve months to finance our operations, fund anticipated capital expenditures, meet our debt obligations and pay dividends. Dividend payments are not guaranteed and our Board of Directors may decide, in its absolute discretion, at any time and for any reason, not to declare or pay further dividends and/or repurchase our common stock. To the extent we undertake future material acquisitions, investments or unanticipated capital expenditures, we may require additional capital. In that context, we regularly evaluate opportunities to enhance our capital structure including through potential debt issuances.

We have drawn on our credit facility from time to time to help us meet financial needs, such as business acquisitions and purchases of common stock under our repurchase program. At March 31, 2015, our available borrowing capacity under the 2014 Credit Facility was $130.7 million. We believe the 2014 Credit Facility will provide us with sufficient flexibility to meet our future financial needs. The credit facility matures in February 2019.

At March 31, 2015, the carrying amount of our debt under the 2014 Credit Facility was $285.8 million. Our average daily borrowings during the three months ended March 31, 2015 were $278.5 million.

Following is a summary of the financial covenants under our credit facility:

Financial Covenant	Requirement	Ratio as of March 31, 2015
Net Leverage Ratio	≤ 3.50 to 1.00	2.19 to 1.00
Interest Coverage Ratio	≥ 2.50 to 1.00	17.97 to 1.00

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Under the 2014 Credit Facility, we also have restrictions on our ability to declare and pay dividends and our ability to repurchase shares of our common stock. In order to pay any cash dividends and/or repurchase shares of stock: (i) no default or event of default shall have occurred and be continuing under the 2014 Credit Facility, and (ii) our pro forma net leverage ratio, as set forth in the credit agreement, must be 0.25 less than the net leverage ratio requirement at the time of dividend declaration or share repurchase. At March 31, 2015, we were in compliance with all debt covenants under the 2014 Credit Facility.

At March 31, 2015, our total cash and cash equivalents balance included approximately $8.5 million of cash that was held by operations outside the U.S. While these funds may not be needed to fund our U.S. operations for at least the next 12 months, if we need these funds, we may be required to accrue and pay taxes to repatriate the funds. Our current plans anticipate repatriating undistributed earnings in Canada. We currently do not intend nor anticipate a need to repatriate our other cash held outside the U.S.

Operating cash flow

Net cash provided by operating activities of $4.2 million decreased by $9.0 million during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to a decrease in cash flow from operations associated with working capital. Throughout both periods, our cash flows from operations were derived principally from: (i) our earnings from on-going operations prior to non-cash expenses such as depreciation, amortization, stock-based compensation and adjustments to our provision for sales returns and allowances; and (ii) changes in our working capital.

Working capital changes are composed of changes in accounts receivable, prepaid expenses and other assets, trade accounts payable, accrued expenses and other liabilities, and deferred revenue. Cash flow from operations associated with working capital decreased $12.1 million during the three months ended March 31, 2015, when compared to the same period in 2014, primarily due to:

- a change in the timing of payouts for certain bonus plans, from quarterly to annually, and an increase in amounts paid resulting from over-performance against 2014 targets; and
- the payout of commissions accrued as of December 31, 2014 which increased, when compared to the same period in 2013, due to an increase in commissionable revenue.

Investing cash flow

During the three months ended March 31, 2015, we had cash outlays of $5.7 million for purchases of property and equipment and software development costs, down from $7.3 million spent during the same period in 2014.

Financing cash flow

During the three months ended March 31, 2015, we increased net borrowings by $5.1 million compared to $19.6 million of net proceeds when we refinanced our debt during the same period in 2014. Also during the three months ended March 31, 2015, we paid dividends of $5.6 million, which was relatively consistent with the amount paid in the comparable period of 2014.

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Item 2. Management's discussion and analysis of financial condition and results of operations (continued)

Commitments and contingencies

As of March 31, 2015, we had future minimum commitments as follows:

	Payments due by period				
(in millions)	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Operating leases[1]	$92.5	$12.8	$23.8	$22.7	$33.2
Debt and interest[2]	310.2	11.2	20.2	278.8	—
Purchase obligations[3]	14.5	9.9	4.5	0.1	—
Total	$417.2	$33.9	$48.5	$301.6	$33.2

(1) Our commitments related to operating leases have not been reduced by incentive payments and reimbursement of leasehold improvements.

(2) Included in the table above is $22.6 million of interest. The actual interest expense recognized in our consolidated statements of comprehensive income will depend on the amount of debt, the length of time the debt is outstanding and the interest rate, which could be different from our assumptions used in the above table, which include: (i) that the amounts outstanding under the 2014 Credit Facility at March 31, 2015 will remain outstanding until maturity, with minimum payments occurring as currently scheduled, and (ii) that there are no assumed future borrowings on the 2014 Revolving Facility for the purposes of determining minimum commitment amounts.

(3) We utilize third-party technology in conjunction with our products and services, with contractual arrangements varying in length from one to five years. In certain cases, these arrangements require a minimum annual purchase commitment by us.

The term loan under the 2014 Credit Facility requires periodic principal payments. The balance of the term loans and any amounts drawn on the revolving credit loans are due upon maturity of the 2014 Credit Facility in February 2019.

The total liability for uncertain tax positions as of March 31, 2015 and December 31, 2014, was $3.1 million and $3.6 million, respectively. Our accrued interest and penalties related to tax positions taken on our tax returns was insignificant as of March 31, 2015 and December 31, 2014.

In February 2015, our Board of Directors approved our annual dividend rate of $0.48 per share to be made in quarterly payments. Dividends at this annual rate would aggregate to $22.6 million assuming 47.0 million shares of common stock are outstanding, although dividends are not guaranteed and our Board of Directors may decide to change or suspend dividend payments at any time for any reason. Our ability to continue to declare and pay dividends quarterly this year and beyond might be restricted by, among other things, the terms of the 2014 Credit Facility, general economic conditions and our ability to generate adequate operating cash flow.

Off-balance sheet arrangements

As of March 31, 2015, we did not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Regulation S-K promulgated by the SEC, that have or are reasonably likely to have, a current or future effect on our financial condition, changes in our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Foreign currency exchange rates

Approximately 11% of our total net revenue for the three months ended March 31, 2015 was derived from operations outside the United States. We do not have significant operations in countries in which the economy is considered to be highly inflationary. Our consolidated financial statements are denominated in U.S. dollars and, accordingly, changes in the exchange rate between foreign currencies and the U.S. dollar will affect the translation of our subsidiaries' financial results into U.S. dollars for purposes of reporting our consolidated financial results. The accumulated currency translation adjustment, recorded within other comprehensive loss as a component of stockholders' equity, was a loss of $1.2 million and $0.9 million as of March 31, 2015 and December 31, 2014, respectively.

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The vast majority of our contracts are entered into by our U.S. or U.K. entities. The contracts entered into by the U.S. entity are almost always denominated in U.S. dollars or Canadian dollars, and contracts entered into by our U.K., Australian, Irish and Netherlands subsidiaries are generally denominated in Pounds Sterling, Australian dollars and Euros, respectively. Historically, as the U.S. dollar weakened, foreign currency translation resulted in an increase in our revenues and expenses denominated in non-U.S. currencies. Conversely, as the U.S. dollar strengthened, foreign currency translation resulted in a decrease in our revenue and expenses denominated in non-U.S. currencies. During the three months ended March 31, 2015, foreign translation resulted in a decrease in our revenues and expenses denominated in non-U.S. currencies. Though we have exposure to fluctuations in currency exchange rates, primarily those between the U.S. dollar and Canadian dollar, the impact was not material to our consolidated results of operations or financial position as of and for the three months ended March 31, 2015. We will continue monitoring such exposure and take action as appropriate.

Inflation

We do not believe that inflation has had a material effect on our business, financial condition or results of operations. If our costs were to become subject to significant inflationary pressures, we may not be able to fully offset such higher costs through price increases. Our inability or failure to do so could harm our business, financial condition and results of operations. In addition, if inflationary pressures impact the rate of giving to our customers, there could be adverse impacts to our business, financial condition and results of operations.

Critical accounting policies and estimates

There have been no significant changes in our critical accounting policies and estimates during the three months ended March 31, 2015 as compared to those disclosed in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014.

Recently issued accounting pronouncements

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-05, Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40) - Customer's Accounting for Fees Paid in a Cloud Computing Arrangement (ASU 2015-05). The amendments in this update provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, the update specifies that the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. The update further specifies that the customer should account for a cloud computing arrangement as a service contract if the arrangement does not include a software license. ASU 2015-05 will be effective for the Company in fiscal year 2016. Early adoption is permitted. An entity can elect to adopt the amendments either (1) prospectively to all arrangements entered into or materially modified after the effective date or (2) retrospectively. We are currently evaluating implementation methods and the extent of the impact that implementation of this standard will have upon adoption.

In April 2015, the FASB issued ASU 2015-03, Interest - Imputation of Interest - Simplifying the Presentation of Debt Issuance Costs. ASU 2015-03 sets forth a requirement that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs is not affected by the amendments in this update. ASU 2015-03 will be effective for the Company in fiscal year 2016. Early adoption is permitted. An entity should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented is adjusted to reflect the period-specific effects of applying the new guidance. We are currently evaluating the extent of the impact that implementation of this standard will have on adoption; however, we will reclassify debt issuance costs from other assets and record them as a direct deduction from the carrying amount of our debt liability.

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In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and will replace most existing revenue recognition guidance in GAAP when it becomes effective. ASU 2014-09 is effective for fiscal years and interim periods within those years beginning after December 15, 2016. Early adoption is not permitted. An entity should apply ASU 2014-09 either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the ASU recognized as an adjustment to the opening balance of retained earnings at the date of initial application. On April 29, 2015, the FASB issued a proposed ASU to defer the effective date of the new standard for one year. The proposal would now require application of the new standard no later than annual reporting periods beginning after December 15, 2017, including interim reporting periods therein; however, under the proposal, public entities would be permitted to elect to early adopt the new standard as of the original effective date. We expect the adoption of ASU 2014-09 will impact our consolidated financial statements. We are currently evaluating implementation methods and the extent of the impact that implementation of this standard will have upon adoption.

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Blackbaud, Inc.

Item 3. Quantitative and qualitative disclosures about market risk

We have market rate sensitivity for interest rates and foreign currency exchange rates.

Interest rate risk

Our variable rate debt is our primary financial instrument with market risk exposure for changing interest rates. We manage interest rate risk through a combination of short-term and long-term borrowings and the use of derivative instruments entered into for hedging purposes. Due to the nature of our debt, the materiality of the fair values of the derivative instruments and the highly liquid, short-term nature and level of our cash and cash equivalents as of March 31, 2015, we believe there is no material risk of exposure to changing interest rates for those positions. There were no significant changes in how we manage interest rate risk between December 31, 2014 and March 31, 2015.

Foreign currency risk

For a discussion of our exposure to foreign currency exchange rate fluctuations, see “Management’s discussion and analysis of financial condition and results of operations — Foreign currency exchange rates” in this report.

Item 4. Controls and procedures

Evaluation of disclosure controls and procedures

Disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e) and 15d-15(e)) are designed only to provide reasonable assurance that they will meet their objectives. As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial and accounting officer), of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e)) pursuant to Exchange Act Rule 13a-15(b). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective to provide the reasonable assurance discussed above.

Changes in internal control over financial reporting

No change in internal control over financial reporting occurred during the most recent fiscal quarter ended March 31, 2015 with respect to our operations, which has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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Blackbaud, Inc.

PART II. OTHER INFORMATION

Item 2. Unregistered sales of equity securities and use of proceeds

Common stock acquisitions and repurchases

The following table provides information about shares of common stock acquired or repurchased during the three months ended March 31, 2015. All of these acquisitions were of common stock withheld by us to satisfy minimum tax obligations of employees due upon exercise of stock appreciation rights and vesting of restricted stock awards and units. The level of acquisition activity varies from period to period based upon the timing of grants and vesting as well as employee exercise decisions.

Period	Total number of shares acquired	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs[(1)]	Approximate dollar value of shares that may yet be purchased under the plans or programs (in thousands)
Beginning balance, January 1, 2015				$50,000
January 1, 2015 through January 31, 2015	1,342	$42.61	$—	50,000
February 1, 2015 through February 28, 2015	32,909	44.73	$—	50,000
March 1, 2015 through March 31, 2015	1,484	46.91	$—	50,000
Total	35,735	$44.74	$—	$50,000

(1) In August 2010, our Board of Directors approved a stock repurchase program that authorized us to purchase up to $50.0 million of our outstanding shares of common stock. We have not made any repurchases under the program to date, and the program does not have an expiration date.

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Blackbaud, Inc.

Item 6. Exhibits

The exhibits listed below are filed or incorporated by reference as part of this Quarterly Report on Form 10-Q:

Exhibit Number	Description of Document	Filed In Filed Herewith	Form	Exhibit Number	Filing Date
31.1	Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X			
31.2	Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X			
32.1	Certification by the Chief Executive Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			
32.2	Certification by the Chief Financial Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			
101.INS*	XBRL Instance Document.	X			
101.SCH*	XBRL Taxonomy Extension Schema Document.	X			
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.	X			
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.	X			
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document.	X			
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.	X			

* Pursuant to Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended or otherwise subject to liability of that Section, and shall not be part of any registration statement or other document filed under the Securities Act of 1933, as amended or the Securities Exchange Act of 1934, as amended, except as shall be expressly set forth by specific reference in such filing.

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Blackbaud, Inc.

SIGNATURES

Pursuant to the requirements 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.

BLACKBAUD, INC.

Date: May 6, 2015

By: /s/ Michael P. Gianoni
Michael P. Gianoni
President and Chief Executive Officer
(Principal Executive Officer)

Date: May 6, 2015

By: /s/ Anthony W. Boor
Anthony W. Boor
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)