

BLACKBAUD INC
Form 10-K
February 26, 2014

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

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

For the Fiscal Year ended December 31, 2013
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)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class

Name of Each Exchange on which Registered

Common Stock, \$0.001 Par Value

The NASDAQ Stock Market LLC
(NASDAQ Global Select Market)

Securities Registered Pursuant to Section 12(g) of the Act: None

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

YES NO

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this

Form 10-K.

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

Large accelerated filer Accelerated filer Non-accelerated filer 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

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant on June 28, 2013 (based on the closing sale price of \$32.57 on that date) was approximately \$1,086,346,945. Common stock held by each officer and director and by each person known to the registrant who owned 10% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

The number of shares of the registrant's Common Stock outstanding as of February 12, 2014 was 46,119,969.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for the 2014 Annual Meeting of Stockholders currently scheduled to be held June 23, 2014 are incorporated by reference into Part III hereof. Such definitive Proxy Statement will be filed with the Securities and Exchange Commission no later than 120 days after the conclusion of the registrant's fiscal year ended December 31, 2013.

BLACKBAUD, INC.
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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K 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,” “targets,” “plans,” “anticipate” 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 under “Item 1A. Risk factors” and elsewhere in this report 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

Item 1. Business

Overview

We are the leading global provider of software and related services designed specifically for nonprofit organizations. Our stated company purpose is to power the business of philanthropy from fundraising to outcomes. We strive to help our customers accomplish their missions and are guided by the following corporate values:

- Our people make us great.
- Customers are at the heart of everything we do.
- We must be good stewards of our resources.
- Innovation drives success.
- Our actions are guided by honesty and integrity.
- Service to others makes the world a better place.

Our customers use our products and services to help increase donations, reduce fundraising costs, improve communications with constituents, manage their finances and optimize operations. We have focused solely on the nonprofit market since our incorporation in 1982. At the end of 2013, we had more than 29,000 customers spread over 69 countries. Our customers come from nearly every segment of the nonprofit sector, including education, foundations, health and human services, faith-based, arts and cultural, public and societal benefits, environment and animal welfare, as well as international and foreign affairs.

Nonprofit Industry

The nonprofit industry is large and diverse

There were more than 1.6 million U.S. nonprofit organizations registered with the Internal Revenue Service in 2012, including nearly 1.1 million charitable 501(c)(3) organizations - double the number of charities in 1992. We estimate there are approximately another 3 million charities internationally. According to Giving USA 2013, donations to U.S. nonprofit organizations in 2012 were \$316.2 billion, amounting to 2.0% of U.S. GDP, a 3.5% increase from 2011 donations of \$305.5 billion. The compound annual growth rate of donations over the 10-year period from 2002 to 2012 was 3.1%, not adjusted for inflation. These nonprofit organizations also receive fees for services they provide, which are estimated at more than \$1.0 trillion annually.

Traditional methods of fundraising are often costly and inefficient

Many nonprofits use manual methods or stand-alone software applications not designed to manage fundraising. Such methods are often costly and inefficient because of the difficulties in effectively collecting, sharing, and using donation-related information. Furthermore, general purpose and Internet-related software applications frequently have limited functionality and do not efficiently integrate multiple databases. Based on our market research, nearly a

quarter of every dollar donated is used for fundraising expenses alone. Some nonprofit organizations have developed proprietary software, but doing so is expensive, requiring on-site technical personnel for development, implementation and maintenance.

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The nonprofit industry faces particular operational challenges
Nonprofit organizations must efficiently:

- Solicit funds and build relationships with major donors;
- Garner small cash contributions from numerous contributors;
- Manage and develop complex relationships with large numbers of constituents;
- Communicate their accomplishments and the importance of their mission online and offline;
- Comply with complex accounting, tax and reporting requirements that differ from those for traditional businesses;
- Solicit cash and in-kind contributions from businesses to help raise money or deliver products and services;
- Provide a wide array of programs and services to individual constituents; and
- Improve the data collection and information sharing capabilities of their employees, volunteers and donors by creating and providing distributed access to centralized databases.

Because of these challenges, we believe nonprofit organizations can benefit from software applications specifically designed to serve their particular needs.

Blackbaud Solutions

We offer a broad suite of products and services that address the fundraising needs and operational challenges facing nonprofit organizations. We provide our customers with cloud-based and on-premise software and related services that help them increase donations, reduce the overall costs of managing their businesses and build a strong sense of community while effectively managing communications with their constituents. We also offer a suite of analytical tools and related services that enable nonprofit organizations to extract, aggregate and analyze vast quantities of data to make better-informed operational decisions. In addition, we help our customers increase the returns on their technology investments by providing a broad range of consulting, training and professional services, maintenance and technical support as well as payment processing services.

Our Strategy

Our objective is to maintain and extend our position as the leading provider of software and related services designed specifically for nonprofit organizations, supporting their missions from fundraising to outcomes. Our key strategies for achieving this objective are to:

Achieve worldwide constituent relationship management (“CRM”) leadership for our CRM products

We offer a range of CRM products which we believe meet the needs of nonprofits of all sizes and across verticals within the nonprofit market. We intend to leverage our CRM portfolio to achieve worldwide leadership in nonprofit CRM by extending the penetration of our CRM product lines to larger, more complex nonprofit organizations, and expanding the reach of our CRM products designed for mid-sized and smaller nonprofits.

Grow our worldwide customer base

We intend to expand our industry-leading customer base and enhance our market position. We have established a strong market presence with more than 29,000 customers. We believe that the fragmented nature of the industry presents an opportunity for us to continue to increase our market penetration. We plan to achieve this by making use of our next generation solutions to continue transforming our business to cloud-based applications, which we expect will allow us to serve the entire mid-market customer segment. We also plan to streamline our sales efforts to the small market customer segment. Additionally, we intend to expand our direct sales efforts, especially with regard to national, enterprise and global account-focused sales teams.

We believe the United Kingdom, Canada, Australia and the Netherlands, as well as other international markets, represent growing market opportunities for our products and services. We believe the overall market of international nonprofit organizations is changing. Donations to international nonprofit organizations are becoming increasingly important in response to reductions in governmental funding. U.S.-based nonprofit organizations are growing their international activities and opening overseas locations. We believe the international marketplace is currently underserved, and we intend to increase our presence by expanding our sales and marketing efforts internationally. We plan to sell complementary products and services to our installed base of customers, and we plan to offer new products tailored to international markets, including leveraging our market leading domestic analytics solutions to develop offerings tailored specifically to meet the needs of foreign and multi-national nonprofits.

Revolutionize the customer experience

We intend to make our customers' experience with us effective, efficient and satisfying from their initial interest in our products and services, through their decision to purchase, engage with customer support and utilize product enhancements. We continue to evolve the manner in which we package and sell our offerings to provide higher value combined with flexibility to meet the different needs of our existing and prospective customers. For example, we are increasing the number of our offerings sold under a subscription pricing model, which can make it easier for customers to purchase our solutions. We will continue to focus on providing the highest level of product support while continuing to enhance our existing products and developing new products and services designed to help allow our customers to more effectively achieve their missions.

Strategically pursue partnerships and acquisitions

We intend to continue to selectively pursue acquisitions, to expand existing partnerships and to develop new strategic partnerships to enter new markets and pursue significant untapped opportunities. We intend to develop these alliances with companies that provide us with complementary technology, customers and personnel with significant relevant experience, as well as to increase our access to additional geographic and vertical markets. We have completed significant acquisitions over the past five years both in the United States and internationally, including the acquisition of Convio, Inc. (Convio) in May 2012. The acquisition of Convio provided us with expanded subscription and online offerings and has accelerated our evolution to a subscription-based revenue model.

We are also currently involved in a number of strategic relationships which allow us to provide a wider variety of offerings and provide customers with integrated solutions, further enhancing the value of our proprietary technology. We believe that our size and history of leadership in the nonprofit sector make us an attractive acquirer or partner for others in the industry.

Our Operating Structure

The nonprofit market is very diverse, with organizations that range from small, local charities to large, multinational relief organizations. The needs of nonprofits can vary greatly according to their size and function. To better serve the wide variety of nonprofits in the market, we organize our operating structure into four operating units: the Enterprise Customer Business Unit, or ECBU, the General Markets Business Unit, or GMBU, the International Business Unit, or IBU, and Target Analytics.

Following is a description of each of our operating units, each of which is a reportable segment for financial accounting purposes:

• The ECBU is focused on marketing, sales, delivery and support to large and/or strategic customers, specifically identified 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.

• The IBU is focused on marketing, sales, delivery and support to all prospects and customers outside of North America.

• Target Analytics is primarily focused on marketing, sales and delivery of analytic services to all prospects and customers in North America.

Each operating unit contains specialized sales, services, support, marketing, and finance functions. We believe this structure allows us to be more responsive to the needs of fundamentally different customer segments and to focus on developing solutions appropriate for these unique markets while leveraging the infrastructure of our broader organization and shared technology in a cost-effective manner. It also allows us to develop highly customized approaches to marketing and selling our products in the markets we serve.

Products and Services

We provide cloud-based and on-premise software solutions and related services to our customers. During 2013, we generated revenue in four reportable segments (the ECBU, the GMBU, the IBU and Target Analytics) and in four geographic regions (United States, Canada, Europe and Asia Pacific), as described in more detail in Note 16 of our consolidated financial statements.

Our broad suite of software, services and analytical tools help nonprofit organizations manage the key aspects of their operations. By automating business processes, our products streamline operations for our customers and help to reduce the

overall costs of operating their organizations. We provide solutions that address many of the technological and business process needs of our customers, including:

- Constituent relationship management;
- Financial management and reporting;
- Cost accounting information for projects and grants;
- Integration of financial data and donor information in a centralized system;
- Online fundraising;
- Peer-to-peer fundraising;
- Event, data and information management;
- Student information systems for independent schools and small colleges;
- Ticketing management;
- General admissions management;
- Analytics and prospect research;
- Consulting and educational services; and
- Payment processing and related regulation compliance.

Software products

We provide our wide variety of solutions to nonprofit organizations in several ways. We offer our products as software-as-a-service (“SaaS”), on a perpetual license basis, or as “hosted” software offerings, which can be used individually to help organizations with specific functions, such as fundraising, constituent relationship management, financial management, website management and prospect research, or combined into a fully-integrated suite of tools to help them manage multiple areas of their operations.

Fundraising and Constituent Relationship Management

The Raiser's Edge

The Raiser's Edge is the leading software solution designed to manage a nonprofit organization's constituent relationship management and fundraising activity. It is used by more than 13,000 organizations worldwide and has won four consecutive Campbell Awards for User Satisfaction from 2009 through 2012. The Raiser's Edge enables nonprofit organizations to cultivate lifelong relationships with supporters, and diversify fundraising methods. Constituent relationship management, online fundraising and email marketing are coupled with analytics, data enrichment tools and best practices, in a single solution.

Blackbaud CRM

Blackbaud CRM is a flexible, extensible, scalable and secure web-based CRM solution. It is our lead offering for organizations with complex fundraising needs across all verticals, specializing in supporting sophisticated major giving, membership and high volume direct marketing programs. Blackbaud CRM helps organizations build deeper and more personalized relationships with constituents, build their brand through online engagement and multi-channel communication tools, and more effectively fundraise, leveraging campaign management, business intelligence and analytics. Blackbaud CRM can be sold as an integrated solution with our enterprise online solutions to enable multi-channel marketing, online engagement and event fundraising.

Luminate CRM

Luminate CRM is our preferred fundraising and CRM offering for mid-tier cause and cure nonprofits and is sold as a single integrated solution with Luminate Online. Luminate CRM is built on the Salesforce.com SaaS computing application platform and offers nonprofits an extensible suite via the Salesforce App Exchange for consolidating information and business processes into one system. The core components of Luminate CRM are campaign management, constituent relations, business intelligence and analytics. When combined with Luminate Online, it provides best-in-class functionality to help nonprofits with online fundraising, peer-to-peer event fundraising, email marketing, advocacy and website management.

eTapestry

eTapestry is a SaaS donor management and fundraising solution built specifically for smaller nonprofits. It offers nonprofit organizations a cost-effective way to manage donors, process gifts, create reports, accept online donations and communicate with constituents. eTapestry was built to operate in a hosted environment and to be accessed online. This technology provides a system that is simple to maintain, efficient to operate and is intuitively easy to learn without extensive training.

Online Solutions

Luminate Online

Luminate Online, delivered as SaaS, helps our customers better understand their online supporters, make the right ask at the right time, and raise money online. It includes tools nonprofits need to build online fundraising campaigns as part of an organization's existing website or as a stand-alone fundraising site. Donation forms, gift processing, and tools for communicating through web pages and email give our customers the essentials for building sustainable donor relationships. Customers can also purchase additional modules including TeamRaiser, a leader within events management that allows nonprofits constituents to create personal or team fundraising web pages and send email donation appeals in support of events such as a walks, runs and rides.

Blackbaud NetCommunity

Blackbaud NetCommunity is an Internet marketing and communications tool that enables organizations that utilize the Raiser's Edge software to build interactive websites and manage email marketing campaigns. With Blackbaud NetCommunity, organizations can, among other things, establish online communities for social networking among constituents and also provide a platform for online giving, membership purchases and event registration. Because Blackbaud NetCommunity requires the Raiser's Edge database to operate, it can only be sold with Raiser's Edge or to existing Raiser's Edge customers. However, Blackbaud NetCommunity, in concert with The Raiser's Edge, provides a single source of up-to-date constituent information across an entire organization, regardless of how individual constituents interact and communicate with the organization.

Sphere eMarketing

Sphere eMarketing, delivered as SaaS, provides organizations with an integrated system of applications to manage e-marketing, communications, programs, services and online fundraising. Sphere eMarketing enables an organization's volunteers, members, donors and staff to share real-time data and information in an online community in order to better manage constituent relationships. Sphere eMarketing is designed to help organizations manage sophisticated and targeted e-mail campaigns with efficiency and control. Comprehensive real-time reports are available to help organizations make strategic data-driven decisions for future marketing campaigns.

Everyday Hero

Everyday Hero is an event-driven web-based fundraising solution in Asia-Pacific and the UK. The Everyday Hero solution is focused on meeting the peer-to-peer fundraising needs of nonprofits internationally. It is a leading donor acquisition tool, and helps nonprofits in Asia-Pacific and the UK connect with a younger, more online-focused generation of donors, a first step in helping nonprofits develop long-term relationships with their supporters. We currently plan to make Everyday Hero available to nonprofits in the U.S. beginning in 2014.

Online Express

Blackbaud Online Express is a simple, cloud-based online fundraising and marketing tool designed for smaller nonprofit organizations using The Raiser's Edge. Launched in 2013, it provides nonprofits with easy-to-use features and functionality such as email marketing, donation forms, event registrations, and dashboard metrics.

Financial Management

The Financial Edge

The Financial Edge is an accounting solution designed to address the specific accounting, analytical and financial reporting needs of nonprofit organizations. It integrates with The Raiser's Edge to simplify gift entry processing and relate information from both systems in an informative manner to eliminate redundant tasks. The Financial Edge provides nonprofit organizations with the means to help manage fiscal and fiduciary responsibility, enabling them to be more accountable to their constituents.

School Management

The Education Edge

The Education Edge is a comprehensive student information management system designed principally to organize an independent school's admissions and registrar processes, including capturing detailed student information, creating class schedules, managing attendance and performance/grades records, producing demographic, statistic, and analytical reports and printing report cards and transcripts.

Blackbaud's Student Information System

Blackbaud's Student Information System is a complete software solution designed for small colleges and other institutions of higher education with a full-time enrollment of less than 5,000. The solution links student information across all campus offices and includes functionality designed specifically to organize the admissions and registrar's processes. Blackbaud's Student Information System helps significantly reduce time spent on data maintenance and creation of class schedules and allows institutions to communicate efficiently with prospects, students and alumni.

Ticketing

The Patron Edge

The Patron Edge is a comprehensive ticketing management solution specifically designed to help large or small performing arts organizations, museums, zoos and aquariums increase attendance and revenue. The Patron Edge can be integrated with The Raiser's Edge to allow for a complete profile view of patrons, donors or visitors. The Patron Edge offers a variety of ticketing methods and allows customers to save time and costs by streamlining ticketing, staffing, scheduling, event and membership management and other administrative tasks.

General Admissions Management

Altru

Altru is an arts and cultural solution suite provided to our customers as a SaaS offering. Altru helps general admissions arts and cultural organizations gain a clear, 360-degree view of their organization, operate more efficiently, engage and cultivate patrons and supporters, streamline external and internal communication efforts, and reduce IT costs. It contains tools for constituent and membership management, program sales, retail sales and ticketing, volunteer management, and events management. It also has sophisticated reporting functionality and tools to manage marketing, communications and fundraising.

Events Management

TeamRaiser

TeamRaiser is a complete online fundraising solution that allows nonprofits to tap into the personal networks of their strongest supporters and mobilize volunteers online. Organized around central fundraising events such as runs, walks or rides, it gives nonprofit constituents the ability to create fundraising web pages and send donation appeals via email to their family and friends.

Sphere Friends Asking Friends

Sphere Friends Asking Friends enables organizations to quickly and easily launch and manage online event fundraising websites. Sphere Friends Asking Friends facilitates growth in donations and participation levels by providing participants tools to become fundraisers and recruiters on behalf of nonprofit organizations. It also allows event participants to reach out to their Facebook® and Twitter® networks, expanding the fundraising and marketing potential of virtual events. It is used by organizations of all sizes and budgets to manage regional to national events.

Consulting and education services

Our consultants provide conversion, implementation and customization services for each of our software products.

These services include:

- System implementation, including all aspects of installation and configuration, to ensure a smooth transition from the customer's legacy system and to create a more streamlined business workflow;

Management of the data conversion process to ensure data is a reliable and powerful source of information for an organization;

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- Business process analysis and application customization to ensure that the organization's system is properly aligned with an organization's processes and objectives;
- Removal of duplicate records, database merging and enrichment, information cleansing and consolidation, and secure credit card transaction processing;
- Database production activities, including direct marketing, business intelligence, cultivation and stewardship processes; and
- Website design services, Internet strategy consulting and specialized services, such as email marketing and search engine optimization.

In addition, we apply our industry knowledge and experience, combined with expert knowledge of our products, to evaluate an organization's needs and consult on how to improve a business process. This work is performed by consultants who have extensive and relevant domain experience in all aspects of nonprofit management, accounting, project management and IT services. We believe that no other software company provides this broad a range of consulting and technology services and solutions dedicated to the nonprofit industry.

We provide a variety of classroom, onsite, distance-learning and self-paced training services to our customers relating to the use of our software products and application of best practices. Our software instructors have extensive training in the use of our software and present course material that is designed to include hands-on lab exercises, as well as course materials with examples and problems to solve.

Analytics services

Target Analytics provides comprehensive solutions for donor acquisition, prospect research, data enrichment, and performance management, enabling nonprofits to define effective campaign strategies and maximize fundraising results. Target Analytics offers services, software, analytics and data within the following areas:

Donor Acquisition - Target Analytics leverages unique data assets to create acquisition mailing lists and predictive models that identify donor populations that meet the affinity, value and response criteria of our nonprofit clients. Nonprofit organizations use our prospect lists to solicit gifts and other support.

Prospect Research - Nonprofit organizations use Target Analytics' prospect research solutions to develop major gift and personal fundraising cultivation strategies. Prospect research solutions include: custom data modeling that delivers critical information on a prospect's likelihood to make a gift to an organization; wealth screenings that deliver detailed wealth information and giving capacity data on prospects; and web-based prospect management software that combines public data with donor information from a nonprofit's database to build a complete view of prospects for targeting and securing gifts.

Data Enrichment - Target Analytics Data Enrichment Services enhance the quality of the data in our customers' databases. Services include: identifying outdated address files in the database and making corrections based on the requirements and certifications of the United States Postal Service, as well as appending data by using known fields in an organization's constituent records to search and identify key demographic and contact information.

Performance Management - Target Analytics creates relevant and insightful reports that benchmark performance and illustrate key industry trends based on performance attributes provided by our nonprofit clients. Nonprofit organizations use our performance and industry analysis reports to assess marketing and operational effectiveness and also to influence operational planning.

Maintenance

Most of our customers that license our software products enroll in one of our maintenance and support programs. In each of the past five years, approximately 95% of our customers have renewed their maintenance plans. Customers enrolled in the programs enjoy fast, reliable customer support, receive regular software updates, stay up-to-date with support newsletters and have unlimited, around-the-clock access to support resources, including our extensive knowledgebase and forums. Customers who enroll in upgraded maintenance plans receive enhanced benefits such as

call support priority and dedicated support resources.

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Payment processing

Our products provide our customers payment processing capabilities that enable their donors to make donations and purchase goods and services using numerous payment options, including credit card and automated clearing house (“ACH”) checking transactions, through secure online transactions. Blackbaud Merchant Services is a value-added service integrated with our solutions that makes credit card processing simple and secure. Customers are charged one rate for transactions, with no extra fees, making Blackbaud Merchant Services a competitive option. The service also provides customers with a payment card industry (“PCI”) compliant process and streamlined bank reconciliation.

Customers

We have customers in every principal vertical market within the nonprofit industry. At the end of 2013, we had more than 29,000 active customers ranging from small, local charities, to healthcare and higher education organizations, to the largest national health and human services organizations. Our largest single customer accounted for approximately 1% of our 2013 consolidated revenue.

Sales and Marketing

The majority of our software and related services are sold through our direct sales force. Our direct sales force is complemented by a team of account development representatives responsible for sales lead generation and qualification. These sales and marketing professionals are located throughout the United States, United Kingdom, the Netherlands, Canada, Australia and New Zealand. As of December 31, 2013, we had 271 direct sales employees. We plan to continue expanding our direct sales force in the Americas, Europe, Australia and Asia as our operations grow internationally and market demand continues to recover from the current economic environment.

We generally begin a customer relationship with the sale of one of our primary products or services, such as The Raiser's Edge, Blackbaud CRM or Luminare, and then offer additional products and services to the customer as the organization's needs increase.

We conduct marketing programs to create brand recognition and market awareness for our products and services. Our marketing efforts include participation at tradeshow, technical conferences and technology seminars, publication of technical and educational articles in industry journals and preparation of competitive analyses. Our customers and strategic partners provide references and recommendations that we often feature in our advertising and promotional activities.

We believe relationships with third parties can enhance our sales and marketing efforts. We have and will continue to establish additional relationships with companies that provide services to the nonprofit industry, such as consultants, educators, publishers, financial service providers, complementary technology providers and data providers. These companies promote or complement our nonprofit solutions and provide us access to new customers.

Corporate Philanthropy and Volunteerism

We believe that service to others makes the world a better place and champion this value through our global corporate philanthropy and employee-volunteer programs. In addition to having employees select grant recipients for our endowment fund, we celebrate individual acts of service through a competitive grant program that honors excellent examples of volunteerism and benefits the organizations they serve.

Competition

The market for software and related services in the nonprofit sector is highly competitive and fragmented. For certain areas of the market, entry barriers are low. However, we believe our experience and product depth makes us a strong competitor. We expect to continue to see new competitors as the market matures and as nonprofit organizations become more aware of the advantages and efficiencies attainable through the use of specialized software. A number of diversified software enterprises have made acquisitions or developed products for the market, including Ellucian, Abila (formerly Sage Nonprofit Solutions), FrontStream Payments, Bloomerang and Campus Management. Other companies that compete with us, such as Microsoft, Salesforce.com and Oracle, have greater marketing resources, revenue and market recognition than we do. They offer some products that are designed specifically for nonprofits, in

addition to some of their products which have a degree of functionality for nonprofits that could be considered competitive. These larger companies could decide to focus more on the nonprofit sector with new, directly competitive products or through acquisitions of our current competitors.

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We mainly face competition from four sources:

- Software developers offering specialized products designed to address specific needs of nonprofit organizations, some of which are sold with subscription pricing;

- Providers of traditional, less automated fundraising services, such as services that support traditional direct mail campaigns, special events fundraising, telemarketing and personal solicitations;

- Custom-developed products created either internally or outsourced to custom service providers; and

- Software developers offering general products not designed to address specific needs of nonprofit organizations.

We compete with several software developers that provide specialized products, such as on-demand software specifically designed for nonprofit use. In addition, we compete with custom-developed solutions created either internally by nonprofit organizations or outside by custom service providers. We believe that we compete successfully, because building efficient, highly functional custom solutions equal to ours requires technical resources that are beyond the capabilities of custom solution providers or require resources that might not be available within nonprofit organizations. In addition, the nonprofit organization's legacy database and software system may not have been designed to support the increasingly complex and advanced needs of today's growing community of nonprofit organizations.

We also compete with providers of traditional, less automated fundraising services, including parties providing services in support of traditional direct mail campaigns, special events fundraising, peer to peer, telemarketing and personal solicitations. Although there are numerous general software developers marketing products that have some application in the nonprofit market, these competitors have generally neglected to focus specifically on this market and typically lack the domain expertise to cost effectively build or implement integrated solutions for the market's needs. We believe we compete successfully against these traditional fundraising services, primarily because our products and services are more automated, more robust, more tailored to the needs of nonprofits and more efficient.

Research and Development

We have made substantial investments in research and development and expect to continue to do so as a part of our strategy to introduce additional products and services. As of December 31, 2013, we had 464 employees working on research and development. Our research and development expenses for 2013, 2012 and 2011 were \$65.6 million, \$64.7 million and \$47.7 million, respectively.

Technology and Architecture

We have products, such as Blackbaud CRM, that are built on the Microsoft.Net framework platform. These products are web-delivered applications utilizing a Service Oriented Architecture built on Internet standards and protocols such as HTTP, XML and SOAP. This architecture is designed to support flexible deployment scenarios including on-premise, hosted applications, and SaaS. The applications expose web service application programming interfaces so that functionality and business logic can be accessed programmatically from outside the context of an interactive user application.

Each of our Luminate products, including Luminate Online, Luminate CRM and TeamRaiser, are SaaS applications that are open and extensible and employ a multi-tenant architecture requiring only a web browser for client access. Luminate Online and TeamRaiser share a common codebase and database, and are built on the Java runtime environment. Luminate CRM is built on the Salesforce.com platform.

Our version 7.x generation products (e.g. The Raiser's Edge and Blackbaud CRM) utilize a three-tier client server architecture built on the Microsoft Component Object Model, or COM.

Regardless of product choice, the development strategies of our solutions are designed to be:

- Flexible. Our component-based architecture is programmable and easily customized by our customers without requiring modification of the source code, ensuring that the technology can be extended to accommodate changing demands of our clients and the market.

- Adaptable. The architecture of our applications allows us to easily add features and functionality or to integrate with third-party applications in order to adapt to our customers' needs or market demands.

Scalable. We combine a scalable architecture with the performance, capacity and load balancing of industry-standard web servers and databases used by our customers to ensure that the applications can scale to the needs of larger organizations.

We do and intend to continue to license technologies from third parties that are integrated into our products.

Intellectual Property and Other Proprietary Rights

To protect our intellectual property, we rely on a combination of patent, trademark, copyright, and trade secret laws in various jurisdictions, as well as employee and third-party nondisclosure agreements and confidentiality procedures. We have a number of registered trademarks, including “Blackbaud,” “The Raiser's Edge,” “Blackbaud CRM” and “Luminate.” We have applied for additional trademarks. We currently have two active patents on our technology, and have a total of three pending patent applications.

Employees

As of December 31, 2013, we had 2,666 employees, none of which are represented by unions or are covered by collective bargaining agreements. We are not involved in any material disputes with any of our employees, and we believe that relations with our employees are satisfactory.

Working Capital

For a discussion of our working capital practices, see “Management’s discussion and analysis of financial conditions and results of operations — Liquidity and capital resources” in Item 7 in this report.

Available Information

Our website address is www.blackbaud.com. We make available, free of charge through our website, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as is reasonably practicable after such material is electronically filed with or furnished to the SEC, but other information on our website is not incorporated into this report. The SEC maintains an Internet site that contains these reports at www.sec.gov. The public may read and copy any materials we file with the SEC at the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

Executive Officers of the Registrant

The following table sets forth information concerning our executive officers as of February 15, 2014:

Name	Age	Title
Michael P. Gianoni	53	President and Chief Executive Officer
Anthony W. Boor	51	Senior Vice President and Chief Financial Officer
Charles T. Cumbaa	61	Senior Vice President, New Business Development
Joseph D. Moye	52	President, Enterprise Customer Business Unit
Kevin Mooney	55	President, General Markets Business Unit
Bradley J. Holman	52	President, International Business Unit
John J. Mistretta	58	Senior Vice President of Human Resources

Michael P. Gianoni joined us as President and Chief Executive Officer in January 2014. Prior to joining us, he served as Executive Vice President and Group President, Financial Institutions at Fiserv, Inc., a global technology provider serving the financial services industry, from January 2010 to December 2013. He joined Fiserv as President of its Investment Services division in December 2007, where he was responsible for product, technology, sales, finance, operations and strategy. Mr. Gianoni was Executive Vice President and General Manager of CheckFree Investment Services, which provided investment management solutions to financial services organizations, from June 2006 until December 2007 when CheckFree was acquired by Fiserv. From May 1994 to November 2005, he served as Senior Vice President of DST Systems Inc., a global provider of technology-based service solutions, where he led various divisions focused on developing new platforms while ensuring stronger operational controls. Mr. Gianoni holds an AS in electrical engineering from Waterbury State Technical College, a BS with a business concentration from Charter Oak State College and an MBA from the University of New Haven.

Anthony W. Boor joined us as Senior Vice President and Chief Financial Officer in November 2011 and served as our interim President and Chief Executive Officer from August 2013 to January 2014. Prior to joining us, he served as an executive with Brightpoint, Inc., a global provider of device lifecycle services to the wireless industry, beginning in 1999, most recently as its Executive Vice President, Chief Financial Officer and Treasurer. He also served as the interim President of Europe, Middle East and Africa during Brightpoint's significant restructuring of that region. Mr. Boor served as Director of Business Operations for Brightpoint North America from August 1998 to July 1999. Prior to joining Brightpoint, Mr. Boor was employed in various financial positions with Macmillan Computer Publishing, Inc., a Viacom owned book publishing company specializing in computer hardware and software related topics, Day Dream Publishing, Inc., a publishing company specializing in calendars, posters and time management materials, Ernst & Young LLP, an accounting firm, Expo New Mexico, a state owned fair and expo grounds and live para-mutual horse racing venue, KPMG LLP, an accounting firm, and Ernst & Whinney LLP, an accounting firm. He holds a BS in Accounting from New Mexico State University.

Charles T. Cumbaa has served as our Senior Vice President of New Business Development since May 2012. He joined us in May 2001 and served as Senior Vice President of Products and Services until December 2009. He also served as our President, Enterprise Customer Business Unit from January 2010 to April 2012. Prior to joining us, Mr. Cumbaa was Executive Vice President with Intertech Information Management, a provider of information management solutions, from December 1998 until October 2000. From 1992 until 1998, he was President and Chief Executive Officer of Cognitech, Inc., a software company he founded. From 1984 to 1992 he was Executive Vice President of Sales and Services at Sales Technologies, a sales force automation company. Prior to that, he was employed by McKinsey & Company, a consulting firm. Mr. Cumbaa holds a BA from Mississippi State University and an MBA from Harvard Business School.

Joseph D. Moye has served as our President, Enterprise Customer Business Unit since October 2012. Before joining us, Mr. Moye was President and Chief Executive Officer for Capgemini Government Solutions, a provider of consulting and technology services to government agencies, from October 2009 to October 2012 where he led the company's expansion in the U.S. public sector marketplace. From October 2006 to September 2009, he was Vice President of Capgemini Group. From January 2000 to September 2005, he was President and Chief Executive Officer of Gazelle Consulting, Inc., a branded leader in business intelligence professional services. Gazelle was acquired by Adjoined Consulting in 2005 and Mr. Moye integrated his team, led the combined business intelligence practice of Adjoined and, ultimately Kanbay's practice after its acquisition of Adjoined, prior to Capgemini acquiring Kanbay. Before founding Gazelle Consulting, Mr. Moye held multiple leadership positions with Sequent Computer Systems, a provider of data center systems and solutions, and Unisys, a provider of IT services, software and technology, where he was responsible for leading business units and channels both domestically and internationally. Mr. Moye holds a BS in Business Administration from Florida State University.

Kevin W. Mooney has served as our President, General Markets Business Unit since January 2010. He joined us in July 2008 as our Senior Vice President of Sales & Marketing and Chief Commercial Officer. Before joining Blackbaud, Mr. Mooney was a senior executive at Travelport GDS from August 2007 to May 2008. As Chief Commercial Officer of Travelport GDS, one of the world's largest providers of information services and transaction processing to the travel industry, Mr. Mooney was responsible for global sales, marketing, training, service and support activities. Prior to that he was Chief Financial Officer for Worldspan from March 2005 until it was acquired by Travelport in August 2007. Mr. Mooney has also held key executive positions in the telecommunications industry and he is a member of the Board of Directors of tw telecom inc., a publicly traded managed network services company. Mr. Mooney graduated from Seton Hall University and holds an MBA in Finance from Georgia State University.

Bradley J. Holman, President of the International Business Unit, joined us in November 2010. Prior to joining Blackbaud, Mr. Holman served as Partner and Chief Commercial Officer at ATI Business Group, a Jakarta-based

company that provides outsourcing and technical services to the aviation and travel sectors, from February 2010 to October 2010. Prior to that, from June 2006 to February 2010, Mr. Holman served as President of Travelport's Asia Pacific operations, which provides information services and transaction processing to the travel industry. From July 2001 to May 2006, Mr. Holman held various senior management roles at Travelport, including Senior Vice President of airline services in Asia Pacific and Managing Director of operations in Europe, Middle East and Africa. Mr. Holman holds a BCom. from University of Western Australia.

John J. Mistretta, our Senior Vice President of Human Resources, joined us in August 2005. Prior to joining us, Mr. Mistretta was an Executive Vice President of Human Resources and Alternative Businesses at National Commerce Financial Corporation, a financial services company, from 1998 to 2005. Earlier in his career, Mr. Mistretta held various senior Human Resources positions over a thirteen year period at the banking firm Citicorp. Mr. Mistretta holds a MS in Counseling and a BA in Psychology from the State University of New York at Oswego.

Item 1A. Risk factors

Our business operations face a number of risks. These risks should be read and considered with other information provided in this report.

General economic factors, both domestically and internationally, might adversely affect our financial performance. General economic conditions, globally or in one or more of the markets we serve, might adversely affect our financial performance. Weakness in the financial and housing markets, inflation, higher levels of unemployment, unavailability of consumer credit, higher consumer debt levels, volatility in credit, equity and foreign exchange markets, higher tax rates and other changes in tax laws, overall economic slowdown and other economic factors could adversely affect donations to nonprofits, reducing their revenue and, therefore, possibly their demand for the products and services we sell and lengthen our sales and payment cycles. Higher interest rates, inflation, higher costs of labor, insurance and healthcare, higher tax rates and other changes in tax laws, changes in other laws and regulations and other economic factors in the United States could increase our cost of sales and operating, selling, general and administrative expenses and otherwise adversely affect our operations and operating results. These factors affect not only our operations, but also the operations of suppliers from whom we purchase or license products and services, a factor that could result in an increase in the cost to us of our products and services, reducing our margins. These factors also affect our customers who may reduce their purchasing of our solutions due to adverse effects of certain economic factors.

We significantly increased our leverage in connection with acquisitions

We incurred a substantial amount of indebtedness in connection with recent acquisitions. As a result of this indebtedness, our interest payment obligations have increased. The degree to which we are leveraged could have adverse effects on our business, including the following:

- Requiring us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures, acquisitions, dividends and other general corporate purposes;
 - Limiting our flexibility in planning for, or reacting to, changes in our business and the industries in which we operate;
 - Restricting us from making additional strategic acquisitions or exploiting business opportunities;
 - Placing us at a competitive disadvantage compared to our competitors that have less debt;
 - Limiting our ability to borrow additional funds; and
 - Decreasing our ability to compete effectively or operate successfully under adverse economic and industry conditions.
- If we incur additional debt, these risks will intensify. Our ability to meet our debt service obligations will depend upon our future performance, which will be subject to the financial, business and other factors affecting our operations, many of which are beyond our control.

Our failure to compete successfully could cause our revenue or market share to decline.

Our market is fragmented, highly competitive and rapidly evolving and there are limited barriers to entry for some aspects of this market. We mainly face competition from four sources:

- Software developers offering specialized products designed to address specific needs of nonprofit organizations, some of which are sold with subscription pricing;
- Providers of traditional, less automated fundraising services, such as services that support traditional direct mail or email campaigns, special events fundraising, telemarketing and personal solicitations;
- Custom-developed products created either internally or outsourced to custom service providers; and
- Software developers offering general products not designed to address specific needs of nonprofit organizations.

The companies we compete with and other potential competitors may have greater financial, technical and marketing resources and generate greater revenue and better name recognition than we do. Companies such as Microsoft, Salesforce.com and Oracle offer some products that are designed specifically for nonprofit organizations, in addition to some of their products

which have a degree of functionality for nonprofit organizations that could be considered competitive. Also, if one or more of our competitors or potential competitors were to merge or partner with one of our other competitors, the change in the competitive landscape could adversely affect our ability to compete effectively. For example, a large diversified software enterprise, such as Microsoft, Oracle or Salesforce.com, could decide to enter the market directly, including through acquisitions. Competitive pressures can adversely impact our business by limiting the prices we can charge our customers and making the adoption and renewal of our solutions more difficult.

Our competitors might also establish or strengthen cooperative relationships with resellers and third-party consulting firms or other parties with whom we have had relationships, thereby limiting our ability to promote our products. These competitive pressures could cause our revenue and market share to decline.

A substantial portion of our revenue is currently derived from The Raiser's Edge, Luminate Online, Blackbaud CRM and The Financial Edge, and a decline in sales or renewals of these or similar products and related services could harm our business.

We derive a substantial portion of our revenue from the sale of The Raiser's Edge, Luminate Online, Blackbaud CRM and The Financial Edge, and other products that help customers manage constituent relationships and related services, and we expect revenue from these products and related services to continue to account for a substantial portion of our total revenue for the foreseeable future. For example, revenue from the sale of The Raiser's Edge and related services represented approximately 28%, 30% and 35% of our total revenue in 2013, 2012 and 2011, respectively. Because we often sell licenses to our products on a perpetual basis and deliver new versions and enhancements to customers who purchase annual maintenance and support, our future license, services and maintenance revenue are substantially dependent on sales to new customers. On the other hand, for our subscription products, we sell our software on an annual or multiyear basis and for annualized fees substantially lower than we would charge for a perpetual license for the same product, so that we depend on customer renewals for future revenues. If renewal rates for the products are lower than expected for any reason, our operating results would be materially and adversely affected. In addition, we frequently sell these or similar products to new customers and then attempt to generate incremental revenue from the sale of additional products and services. If demand for The Raiser's Edge, Luminate Online, Blackbaud CRM, The Financial Edge or similar products declines significantly, our business would suffer.

We encounter lengthy sales cycles which could have an adverse effect on the amount, timing and predictability of our revenue and sales.

Potential customers, particularly our larger enterprise clients, generally commit significant resources to an evaluation of available software and require us to expend substantial time, effort and money educating them as to the value of our software and services. Sales of our software products to these larger customers often require an extensive education and marketing effort. We could expend significant funds and management resources during the sales cycle and ultimately fail to close the sale. Historically, our software product sales cycle averages approximately two months for sales to existing customers and from six to nine months for sales to new customers. Our sales cycle for all of our products and services is subject to significant risks and delays over which we have little or no control, including:

- Our customers' budgetary constraints;
- The timing of our clients' budget cycles and approval processes;
- The impact of the macroeconomic environment on our customers;
- Our clients' willingness to replace their current methods or software solutions;
- Our need to educate potential customers about the uses and benefits of our products and services; and
- The timing and expiration of our clients' current license agreements or outsourcing agreements for similar services.

If we are unsuccessful in closing sales after expending significant funds and management resources or if we experience delays as discussed above, it could have a material adverse effect on the amount, timing and predictability of our revenue.

We encounter long and complex implementation cycles, particularly for our largest customers, which could have an adverse effect on our profitability and the timing and predictability of our revenue.

The implementation of our products and services, particularly in our large CRM engagements, frequently involves complex configuration, business process reengineering and system interfaces and can extend for a year or more. Our enterprise CRM product offerings are complex and we may not have historical experience with unanticipated

implementation challenges or complexities that could arise in these engagements. Further, these projects typically are heavily dependent on customer

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participation, communication and timely responsiveness throughout the implementation cycle. As the complexity of these engagements increases, our revenues and profitability could suffer from delays in project completion and having to perform unplanned incremental services at rates substantially below our normal hourly rates or make investments in the form of non-billable service hours or other concessions. If we are unsuccessful in implementing our products or if we experience delays, it could have a material adverse effect on our profitability and the timing and predictability of our revenue.

If our customers do not renew their annual maintenance and support agreements or subscriptions for our products or if they do not renew them on terms that are favorable to us, our business might suffer.

Most of our maintenance agreements and subscriptions are for a one year term. As the end of the annual period approaches, we seek the renewal of the agreement with the customer. Historically, maintenance and subscriptions renewals have represented a significant portion of our total revenue. Because of this characteristic of our business, if our customers choose not to renew their maintenance and support agreements or subscriptions with us on beneficial terms or at all, our business, operating results and financial condition could be harmed. Our customers' renewal rates may decline or fluctuate as a result of a number of factors, including their level of satisfaction with our products and services and their ability to continue their operations and spending levels.

We might not generate increased business from our current customers, which could limit our revenue in the future.

Our ability to grow revenue is highly dependent on the success of our efforts to sell additional products and services to our existing customers. Many of our customers initially make a purchase of only one or a limited number of our products or only for a single department within their organization. These customers might choose not to expand their use of or make additional purchases of our products and services. If we fail to generate additional business from our current customers, our revenue could grow at a slower rate or even decrease. In addition, as we deploy new applications and features for our existing products or introduce new products and services, our current customers could choose not to purchase these new offerings.

The offering of our products on a subscription basis is evolving and demand by our customers for these offerings is increasing. Our failure to manage this evolution and demand could lead to lower than expected revenues and profits. In recent years, much of our revenue growth was derived from increased subscription offerings, including SaaS. This business model depends heavily on achieving economies of scale because the initial upfront investment is costly and the associated revenue is recognized on a ratable basis. If we fail to achieve appropriate economies of scale or if we fail to manage or anticipate the evolution and demand for the subscription software pricing models, then our business and operating results could be adversely affected. The additional investments required to meet customer demand will increase our cost base, which will make it more difficult for us to offset any future revenue shortfalls by reducing expenses in the short term.

Defects, delays or interruptions in our SaaS and hosting services could diminish demand for these services and subject us to substantial liability.

We currently utilize data center hosting facilities to provide SaaS and hosting services to our customers. Any damage to, or failure of, our data center systems generally could result in interruptions in service to our customers, notwithstanding any disaster recovery arrangements that may currently be in place at these facilities. Because our SaaS, Internet-based and hosting service offerings are complex, and we have incorporated a variety of new computer hardware and software systems at the data centers, our services might have errors or defects that users identify after they begin using our services. This could result in unanticipated downtime for our customers and harm to our reputation and our business. Internet-based services frequently contain undetected errors when first introduced or when new versions or enhancements are released. We have from time to time found defects in our Internet-based services and new errors might again be detected in the future. In addition, our customers might use our Internet-based offerings in unanticipated ways that cause a disruption in service for other customers attempting to access their data. Because our customers use these services for important aspects of their business, any defects, delays or disruptions in service or other performance problems with our services could hurt our reputation and damage our customers' businesses. If that occurs, customers could elect to cancel their service, or delay or withhold payment to us, we could lose future sales or customers might make claims against us, which could result in an increase in our provision for

doubtful accounts, an increase in collection cycles for accounts receivable or the expense and risk of litigation. Any of these could harm our business and our reputation.

The market for software and services for nonprofit organizations might not grow and nonprofit organizations might not continue to adopt our products and services.

Many nonprofit organizations have not traditionally used integrated and comprehensive software and services for their nonprofit-specific needs. We cannot be certain that the market for such products and services will continue to develop and grow or that nonprofit organizations will elect to adopt our products and services rather than continue to use traditional, less automated methods, attempt to develop software internally, rely upon legacy software systems, or use software solutions not specifically designed for the nonprofit market. Nonprofit organizations that have already invested substantial resources in other fundraising methods or other non-integrated software solutions might be reluctant to adopt our products and services to supplement or replace their existing systems or methods. In addition, the implementation of one or more of our core software products can involve significant time and capital commitments by our customers, which they may be unwilling or unable to make. If demand for and market acceptance of our products and services does not increase, we might not grow our business as we expect.

Because a significant portion of our revenue is recognized ratably over the terms of the contract, downturns in sales may not be immediately reflected in our revenue.

We recognize our maintenance and subscriptions revenue monthly over the term of the customer agreement. The terms of the customer agreements typically range from 1-3 years. As a result, much of the revenue we report in each quarter is attributable to agreements entered into during previous quarters. Consequently, a decline in sales to new customers, renewals by existing customers or market acceptance of our products in any one quarter will not necessarily be fully reflected in the revenues in that quarter and will negatively affect our revenues and profitability in future quarters.

Our operations might be affected by the occurrence of a natural disaster or other catastrophic event.

We depend on our principal executive offices and other facilities for the continued operation of our business.

Although we have contingency plans in effect for natural disasters or other catastrophic events, these events, including terrorist attacks and natural disasters such as hurricanes and earthquakes, could disrupt one or more of these facilities and adversely affect our operations. In addition, our Charleston headquarters require a remediation effort to improve weather resistance. This remediation effort is the responsibility of the landlord, but delays in the remediation or disruption caused by the remediation effort could have an adverse effect on our operations. Even though we carry business interruption insurance policies and typically have provisions in our contracts that protect us in certain events, we might suffer losses as a result of business interruptions that exceed the coverage available under our insurance policies or for which we do not have coverage. Any natural disaster or catastrophic event affecting us could have a significant negative impact on our operations.

If the security of our software is breached, we fail to securely collect, store and transmit customer information, or we fail to safeguard confidential donor data, our products and services might be perceived as not being secure and our reputation and business could suffer.

Fundamental to the use of our products is the secure collection, storage and transmission of confidential donor and end user information. The commercially available network and application security, internal control measures, and physical security procedures to safeguard our systems, may not be sufficient to prevent a security breach, intrusion, loss or theft of personal information will not occur, which may harm our business, customer reputation and future financial results. Any such breach may require us to expend significant resources to address, including notification under data privacy regulations.

Additionally, despite our efforts to combat such measures, computer hackers may attempt to penetrate or bypass our data protection and other security measures and gain unauthorized access to our networks, systems and data or compromise the confidential information of data of our customers. Computer hackers may be able to develop and deploy computer viruses, worms, and other malicious software programs that could attack our products and services, exploit potential security vulnerabilities of our products and services, create system disruptions and cause shutdowns or denials of service. Data may also be accessed or modified improperly as a result of employee or supplier error or malfeasance and third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our data, our customers' data or our IT systems. These risks for us will increase as we continue to grow our cloud-based offerings and services and

store and process increasingly large amounts of our customers' confidential information and data and host or manage parts of our customers' business in cloud-based IT environments, especially in customer sectors involving particularly sensitive data such as health sciences, financial services and the government. We also have an active acquisition program and have acquired a number of companies, products, services and technologies over the years. While we make significant efforts to address any IT security issues with respect to our acquisitions, we may still inherit such risks when we integrate these acquisitions within our business.

A compromise of our software or other problems that results in customer or donor personal information being obtained by unauthorized persons could adversely affect our reputation with our customers and others, as well as our operations, results of operations, financial condition and liquidity and could result in litigation against us or the imposition of penalties. In addition, a security breach could require that we expend significant additional resources related to our information security systems and could result in a disruption of our operations, particularly our online sales operations. The existence of vulnerabilities, even if they do not result in a security breach, may harm customer confidence and require substantial resources to address, and we may not be able to discover or remedy such security vulnerabilities before they are exploited. Also, computers, including those that use our software, are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We might be required to expend significant capital and other resources to protect further against security breaches or to rectify problems caused by any security breach.

Privacy and security concerns, including evolving government regulation in the area of consumer data privacy, could adversely affect our business and operating results.

The effectiveness of our software products relies on our customers' storage and use of data concerning their customers, including financial, personally identifying and other sensitive data. Our customers' collection and use of this data for donor profiling might raise privacy and security concerns and negatively impact the demand for our products and services. For example, our custom modeling and analytical services, including ProspectPoint, WealthPoint and donorCentrics, rely heavily on securing and making use of data we gather from various sources and privacy laws could jeopardize our ability to market and profit from those services. If a breach of customer data security were to occur, our products may be perceived as less desirable, which would negatively affect our business and operating results.

Governments in some jurisdictions have enacted or are considering enacting consumer data privacy legislation, including laws and regulations applying to the solicitation, collection, processing and use of consumer data. This legislation could reduce the demand for our software products if we fail to design or enhance our products to enable our customers to comply with the privacy and security measures required by the legislation. Moreover, we may be exposed to liability under existing or new consumer data privacy legislation. For example, we are subject to the privacy provisions of the Health Insurance Portability and Accountability Act of 1996, or HIPAA, and might be subject to similar provisions of the Gramm-Leach-Bliley Act and related regulations. Even technical violations of these laws can result in penalties that are assessed for each non-compliant transaction. As part of the American Recovery and Reinvestment Act of 2009, Congress passed the Health Information Technology for Economic and Clinical Health Act, or HI-TECH Act. The HI-TECH Act expands the reach of data privacy and security requirements of HIPAA to service providers. HIPAA and associated United States Department of Health and Human Services regulations permit our customers in the healthcare industry to use certain demographic protected health information (such as name, email or physical address and dates of service) for fundraising purposes and to disclose that subset of protected health information to their service providers for fundraising. We may be included in this service provider group under the revised HIPAA regulations by virtue of our service provider relationship with our customers in the healthcare industry. In general, we seek to contractually prohibit our healthcare industry customers from using other types of health information of their clients for fundraising purposes that would be non-compliant with HIPAA, but we believe monitoring our healthcare customers' compliance with such prohibitions is not legally required of service providers and would be cost prohibitive. The law and regulations under HI-TECH are new and still subject to change or interpretation by legal authorities who could cause additional compliance burdens. If we or our customers were found to be subject to and in violation of any of these laws or other data privacy laws or regulations, our business could suffer and we and/or our customers would likely have to change our business practices. In addition, these laws and regulations could impose significant costs on us and our customers and make it more difficult for donors to make online donations.

We are in the information technology business, and our products and services store, retrieve, manipulate and manage our customers' information and data. The effectiveness of our software products relies on our customers' storage and use of data concerning their donors, including financial, personally identifying and other sensitive data and our business uses similar systems that require us to store and use data with respect to our customers and personnel. Our

collection and our customers' collection and use of this data might raise privacy and security concerns and negatively impact our business or the demand for our products and services. If a breach of data security were to occur, our business may be materially and adversely impacted and products may be perceived as less desirable, which would negatively affect our business and operating results.

If we are unable, or customers believe we are unable, to detect and prevent unauthorized use of credit cards and safeguard confidential donor data, we could be subject to financial liability, our reputation could be harmed and customers may be reluctant to use our products and services.

Advances in computer capabilities, new discoveries in the field of cryptography or other events or developments could result in a compromise or breach of the technology we use to protect sensitive transaction data. If any such compromise of our security,

or the security of our customers, were to occur, it could result in misappropriation of proprietary information or interruptions in operations and have an adverse impact on our reputation or the reputation of our customers. All of our products are currently certified as Payment Application Data Security Standard compliant. Currently some of our products are not fully compliant with Payment Card Industry Data Security Standard, or PCI DSS. This or other factors could make customers believe we are unable to detect and prevent unauthorized use of credit cards or confidential donor data, which could harm our business. Additionally, these factors could make issuing banks believe the transactions of our customers are compromised and refuse to process those transactions, which could harm the reputation of our products and our business.

Conforming our products and services to PCI DSS is expensive and time-consuming. Our failure to achieve or maintain compliance with PCI DSS could make customers believe we are unable to detect and prevent unauthorized use of credit cards and bank account numbers or protect confidential donor data and our reputation and business might be harmed.

Our operations process a significant volume and dollar value of transactions on a daily basis, especially in our payroll and payments businesses. Due to the size and volume of transactions that we handle, effective processing systems and controls are essential to ensure that transactions are handled appropriately. Despite our efforts, it is possible that we may make errors or that funds may be misappropriated due to fraud. The systems supporting our business are comprised of multiple technology platforms that are difficult to scale. If we are unable to effectively manage our systems and processes we may be unable to process customer data in an accurate, reliable and timely manner, which may harm our business. In our payments processing services business, if merchants for whom we process payment transactions are unable to pay refunds due to their customers in connection with disputed or fraudulent merchant transactions, we may be required to pay those amounts and our payments may exceed the amount of the customer reserves we have established to make such payments.

As a result of the evolution of our business model to meet customer demand, roughly two thirds of our revenue is now from subscriptions and services, which produces substantially lower gross margins than our traditional license and maintenance revenue. Continuation of this trend will dilute our overall gross margins.

Over the past several years we have evolved our business model toward subscription and service based delivery and away from the traditional software model of perpetual licenses with term-based maintenance. For example, in 2013 our subscription revenue exceeded our combined license and maintenance revenue for the first time, and together subscription and services revenue comprised approximately two thirds of our total revenue. These changes in our model have been driven by customer demand, and we believe have the long-term benefit of producing more predictable and recurring long-term revenue streams. However our subscription and services revenue generate substantially lower gross margins than our product license revenue. For example, in 2013, our subscriptions and services gross margins were 56% and 18%, respectively, whereas for the same period our license and maintenance revenue gross margins were 83% and 81%, respectively. We expect that over time the shift toward subscription and services revenue will continue. If we are unable to achieve economies of scale in our subscription business or increase efficiency in our services business, our overall margins will be adversely affected. Additionally, if nonprofits in general, and specifically our customers and prospects, desire to adopt our subscription offerings much more rapidly than we currently anticipate and we are unable to respond in a timely fashion, we could encounter significant adverse effects to our business, including substantial capital expenditures, reduction in profitability, decrease in revenue growth and/or we could become potentially less competitive, resulting in a loss of market share.

Certain of our services are contracted under fixed fee arrangements, which we base on estimates. If our estimated number of hours to perform engagement implementation services are less than our actual hours, our operating results would be adversely affected. Services revenue as a percentage of total revenue has varied significantly from quarter to quarter due to fluctuations in licensing revenue, economic changes, varying accounting treatments, changes in the average selling prices for our products and services, our customers' acceptance of our products and our sales force execution. In addition, the volume and profitability of services can depend in large part upon:

• Competitive pricing pressure on the rates that we can charge for our services;

The complexity of the customers' information technology environment and the existence of multiple non-integrated legacy databases;

•The resources directed by customers to their implementation projects;

•The extent of software customization included in the implementation projects; and

•The extent to which outside consulting organizations provide services directly to customers.

A decrease in the demand for services could adversely affect our profitability and operating results.

Our quarterly financial results fluctuate and might be difficult to forecast and, if our future results are below either any guidance we might issue or the expectations of public market analysts and investors, the price of our common stock might decline.

Our quarterly revenue and results of operations are difficult to forecast. We have experienced, and expect to continue to experience, fluctuations in revenue and operating results from quarter to quarter. As a result, we believe that quarter-to-quarter comparisons of our revenue and operating results are not necessarily meaningful and that such comparisons might not be accurate indicators of future performance. The reasons for these fluctuations include but are not limited to:

• The size and timing of sales of our software, including the relatively long sales cycles associated with many of our larger software sales;

• Budget and spending decisions by our customers;

• The degree of judgment required to estimate large consulting service engagements;

• Scheduling considerations by our customers as they impact the delivery of purchased services;

• Varying accounting treatments based upon the facts and circumstances of each arrangement;

• Utilization of our professional services personnel;

• Market acceptance of new products we release or acquire;

• Changes in general economic conditions and conditions in the markets we serve;

• Costs related to acquisitions of technologies or businesses;

• The growth rates of certain market segments in which we compete;

• The amount and timing of operating costs and capital expenditures related to the operations and expansion of our business;

• Changes in our pricing policies and terms of contracts, whether initiated by us or as a result of competition;

• The rate of expansion and productivity of our sales force and the impact of reorganizations of our sales force;

• Technical difficulties or interruptions in our service;

• Changes in foreign currency exchange rates;

• Changes in the effective tax rates due to changes in the mix of earnings and losses in countries with differing statutory tax rates, certain non-deductible expenses, changes in the valuation of deferred tax assets and liabilities and our ability to utilize them, changes in federal, state or international tax laws and accounting principles, changes in judgment from the evaluation of new information that results in a recognition, derecognition or change in measurement of a tax position taken in a prior period, results of tax examinations by local and foreign taxing authorities;

• Expenses related to significant, unusual or discrete events which are recorded in the period in which the events occur;

• Regulatory compliance costs; and

• Extraordinary expenses such as litigation or other dispute-related settlement payments.

Many of these factors are outside of our control, and the occurrence of one or more of them might cause our operating results to vary widely. As such, we believe that quarter-to-quarter comparisons of our revenues, operating results, changes in our deferred revenue and unbilled deferred revenue balances and cash flows may not be meaningful and should not be relied upon as an indication of future performance.

Our operating expenses, which include sales and marketing, research and development and general and administrative expenses, are based on our expectations of future revenue and are, to a large extent, fixed in the short term. If revenue falls below our expectations in a quarter and we are not able to quickly reduce our operating expenses in response, our operating results for that quarter could be adversely affected. It is possible that in some future quarter our operating results may be below either any guidance we might issue or the expectations of public market analysts and investors and, as a result, the price of our common stock might fall.

If we fail to respond to technological changes to be competitive, our business could suffer.

The software industry is characterized by technological change, evolving industry standards in hardware and software technology, changes in customer requirements and frequent new product introductions and enhancements. The introduction of

products encompassing new technologies can render existing products obsolete and unmarketable. As a result, our future success will depend, in part, upon our ability to continue to enhance existing products and develop and introduce in a timely manner or acquire new products that keep pace with technological developments, satisfy increasingly sophisticated customer requirements and achieve market acceptance. There is no assurance that we will successfully identify new product opportunities and develop and bring new products to market in a timely and cost-effective manner. Further, there can be no assurance that the products, capabilities or technologies developed by others will not render our products or technologies obsolete or noncompetitive. In addition, because our service is designed to operate on a variety of network hardware and software platforms using a standard browser, we will need to continuously modify and enhance our service to keep pace with changes in Internet-related hardware, software, communication, browser and database technologies. We have made and continue to make significant working capital investments in accordance with evolving industry and customer requirements. These concentrations of working capital increase our risk of loss due to product or technology obsolescence. If we are unable to develop or acquire on a timely and cost-effective basis new software products or enhancements to existing products or if such new products or enhancements do not achieve market acceptance, our business, results of operations and financial condition may be materially adversely affected.

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

To meet our objectives successfully, we must attract and retain highly qualified personnel with specialized skill sets. If we are unable to attract suitably qualified management, there could be a material adverse impact on our business. In addition, to execute our continuing growth plans, we need to increase the size and maintain the quality of our sales force, software development staff and our professional services organization. Competition for qualified personnel can be intense, and we might not be successful in attracting and retaining them. The pool of qualified personnel with experience working with or selling to nonprofit organizations is limited overall and specifically in Charleston, South Carolina, where our principal office is located. Our ability to maintain and expand our sales, product development and professional services teams will depend on our ability to recruit, train and retain top quality people with advanced skills who understand sales to, and the specific needs of, nonprofit organizations. For these reasons, we have from time to time in the past experienced, and we expect to continue to experience in the future, difficulty in hiring and retaining highly skilled employees with appropriate qualifications for our business. In addition, it takes time for our new sales and services personnel to become productive, particularly with respect to obtaining and supporting major customer accounts. We might also engage additional third-party consultants as contractors, which could have a negative impact on our earnings. If we are unable to hire or retain qualified personnel, or if newly hired personnel fail to develop the necessary skills or reach productivity slower than anticipated, it would be more difficult for us to sell our products and services, we could experience a shortfall in revenue or earnings and not achieve our planned growth. Further, in the past, we have used equity incentive programs as part of our overall employee compensation arrangements to both attract and retain personnel. A decline in our stock price could negatively impact the value of these equity incentive and related compensation programs as retention and recruiting tools. We may need to create new or additional equity incentive programs and/or compensation packages to remain competitive, which could be dilutive to our existing stockholders and/or adversely affect our results of operations.

If we do not successfully address the risks inherent in the expansion of our international operations, our business could suffer.

We currently have operations in Canada, United Kingdom, the Netherlands, Ireland, Australia and New Zealand, and we intend to expand further into international markets. We have limited experience in international operations and might not be able to compete effectively in international markets. Our international offices generated revenues of approximately \$63.9 million, \$61.0 million and \$53.6 million for the years ended December 31, 2013, 2012 and 2011, respectively. Accordingly, international revenue increased 4.8% and 13.8% in 2013 and 2012, respectively. Expansion of our international operations will require a significant amount of attention from our management and substantial financial resources and might require us to add qualified management in these markets. Our direct sales model requires us to attract, retain and manage qualified sales personnel capable of selling into markets outside the United States. In some cases, our costs of sales might increase if our customers require us to sell through local distributors.

If we are unable to grow our international operations in a cost effective and timely manner, our business and operating results could be harmed. Doing business internationally involves additional risks that could harm our operating results, including:

- Difficulties associated with and costs of staffing and managing international operations;
- Differing technology standards;
- Difficulties in collecting accounts receivable and longer collection periods;

- Political and economic instability;
- Imposition of currency exchange controls;
- Potentially adverse tax consequences;
- Reduced protection for intellectual property rights in certain countries;
- Dependence on local vendors;
- Protectionist laws and business practices that favor local competition;
- Compliance with multiple conflicting and changing governmental laws and regulations;
- Seasonal reductions in business activity specific to certain markets;
- Longer sales cycles;
- Restrictions on repatriation of earnings or new taxation thereon;
- Differing labor regulations;
- Differing accounting rules and practices;
- Restrictive privacy regulations in different countries, particularly in the European Union;
- Restrictions on the export of technologies such as data security and encryption;
- Compliance with U.S. laws such as the Foreign Corrupt Practices Act, and local laws prohibiting corrupt payments to government officials; and
- Import and export restrictions and tariffs.

We expect that an increasing portion of our international revenues will be denominated in foreign currencies, subjecting us to fluctuations in foreign currency exchange rates. If we expand our international operations, exposures to gains and losses on foreign currency transactions may increase.

Material defects or errors in the software we use to deliver our services could harm our reputation, result in significant costs to us and impair our ability to sell our services.

The software applications underlying our services are inherently complex and may contain material defects or errors, particularly when first introduced or when new versions or enhancements are released. We have from time to time found defects in our service, and new errors in our existing service may be detected in the future. Any defects that cause interruptions to the availability of our services could result in adverse impacts to our business, including:

- A reduction in sales or delay in market acceptance of our services;
- Sales credits or refunds to our customers;
- Loss of existing customers and difficulty in attracting new customers;
- Diversion of development resources;
- Harm to our reputation; and
- Increased warranty and insurance costs.

After the release of our services, defects or errors may also be identified from time to time by our internal team and by our customers. The costs incurred in correcting any material defects or errors in our services may be substantial and could harm our operating results. Furthermore, our customers may use our software together with products from other companies. As a result, when problems occur, it might be difficult to identify the source of the problem. Even when our software does not cause these problems, the existence of these errors might cause us to incur significant costs, divert the attention of our technical personnel from our product development efforts, impact our reputation and cause significant customer relations problems.

Our failure to obtain licenses for third-party technologies could harm our business.

We expect to continue licensing technologies from third parties, including applications used in our research and development activities, technologies which are integrated into our products and products that we resell. We believe that the loss of any third-party technologies currently integrated into our products could have a material adverse effect on our business. Our inability in

the future to obtain any third-party licenses on commercially reasonable terms, or at all, could delay future product development until equivalent technology can be identified, licensed or developed and integrated. This inability in turn would harm our business and operating results. Our use of third-party technologies exposes us to increased risks including, but not limited to, risks associated with the integration of new technology into our products, the diversion of our resources from development of our own proprietary technology and our inability to generate revenue from licensed technology sufficient to offset associated acquisition and maintenance costs.

Claims that we or our technologies infringe upon the intellectual property or other proprietary rights of a third party may require us to incur significant costs, enter into royalty or licensing agreements or develop or license substitute technology.

We may in the future be subject to claims that our technologies in our products and services infringe upon the intellectual property or other proprietary rights of a third party. In addition, the vendors providing us with technology that we use in our own technology could become subject to similar infringement claims. Although we believe that our products and services do not infringe any intellectual property or other proprietary rights, we cannot be certain that our products and services do not, or that they will not in the future, infringe intellectual property or other proprietary rights held by others. Any claims of infringement could cause us to incur substantial costs defending against the claim, even if the claim is without merit, and could distract our management from our business. Moreover, any settlement or adverse judgment resulting from the claim could require us to pay substantial amounts, or obtain a license to continue to use the products and services that are the subject of the claim, and/or otherwise restrict or prohibit our use of the technology. There can be no assurance that we would be able to obtain a license on commercially reasonable terms from the third party asserting any particular claim, or that we would be able to successfully develop alternative technology on a timely basis, or that we would be able to obtain a license from another provider of suitable alternative technology to permit us to continue offering, and our customers to continue using, the products and services. In addition, we generally provide in our customer agreements for certain products and services that we will indemnify our customers against third-party infringement claims relating to technology we provide to those customers, which could obligate us to pay damages if the products and services were found to be infringing. Infringement claims asserted against us, our vendors or our customers may have a material adverse effect on our business, prospects, financial condition and results of operations.

Our solutions utilize open source software, which may subject us to litigation, require us to re-engineer our solutions, or otherwise divert resources away from our development efforts.

We use open source software in connection with certain of our solutions. Such open source software is generally licensed by its authors or other third parties under open source licenses, including, for example, the GNU General Public License, the GNU Lesser General Public License, "Apache-style" licenses, "BSD-style" licenses and other open source licenses. There is little legal precedent governing the interpretation of many of the terms of some of these licenses, and therefore the potential impact of these terms on our business is currently unable to be determined and may result in unanticipated obligations regarding our products and technologies. From time to time, companies that incorporate open source software into their products have faced claims challenging the ownership of open source software and/or compliance with open source license terms. Therefore, we could be subject to litigation by parties claiming ownership of open source software or noncompliance with open source licensing terms. Some open source software licenses require users who distribute open source software as part of their own software to publicly disclose all or part of the source code to such software and/or make available any derivative works of the open source code on unfavorable terms or at no cost. While we monitor our use of open source software and try to ensure that none is used in a manner that would require us to disclose the source code or that would otherwise breach the terms of an open source agreement, such use could inadvertently occur and we may be required to release proprietary source code, pay damages for breach of contract, re-engineer our applications, discontinue sales in the event re-engineering cannot be accomplished on a timely basis, or take other remedial action that may divert resources away from our development efforts, any of which could adversely affect our business.

We rely upon trademark, copyright, patent and trade secret laws to protect our proprietary rights, which might not provide us with adequate protection.

Our success and ability to compete depends to a significant degree upon the protection of our software and other proprietary technology rights. We might not be successful in protecting our proprietary technology and our proprietary rights might not provide us with a meaningful competitive advantage. To protect our core proprietary technology, we rely on a combination of patent, trademark, copyright and trade secret laws, as well as nondisclosure agreements, each of which affords only limited protection. We have no patent protection for The Raiser's Edge, which is one of our core products and responsible for a significant portion of our revenue. Any inability to protect our intellectual property rights could seriously harm our business, operating results and financial condition. It is possible that:

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• Any patents issued to us may not be timely or broad enough to protect our proprietary rights;
• Any issued patent could be successfully challenged by one or more third parties, which could result in our loss of the right to prevent others from exploiting the inventions claimed in those patents; and
• Current and future competitors may independently develop similar technologies, duplicate our products or design around any of our patents.

In addition, the laws of some foreign countries do not protect our proprietary rights in our products to the same extent as do the laws of the United States. Despite the measures taken by us, it may be possible for a third party to copy or otherwise obtain and use our proprietary technology and information without authorization. Policing unauthorized use of our products is difficult, and litigation could become necessary in the future to enforce our intellectual property rights. Any litigation could be time consuming and expensive to prosecute or resolve, and could result in substantial diversion of management attention and resources and materially harm our business, financial condition and results of operations.

Restrictions in our revolving credit facility may limit our activities, including dividend payments, share repurchases and acquisitions.

Our credit facility contains restrictions, including covenants limiting our ability to incur additional debt, grant liens, make acquisitions and other investments, prepay specified debt, consolidate, merge or acquire other businesses, sell assets, pay dividends and other distributions, repurchase stock and enter into transactions with affiliates. There can be no assurance that we will be able to remain in compliance with the covenants to which we are subject in the future and, if we fail to do so, that we will be able to obtain waivers from our lenders or amend the covenants.

In the event of a default under our credit facility, we could be required to immediately repay all outstanding borrowings, which we might not be able to do. In addition, certain of our material domestic subsidiaries will be required to guarantee amounts borrowed under the credit facility, and we have pledged the shares of certain of our subsidiaries as collateral for our obligations under the credit facility. Any such default could have a material adverse effect on our ability to operate, including allowing lenders under the credit facility to enforce guarantees of our subsidiaries, if any, or exercise their rights with respect to the shares pledged as collateral.

Our business and financial performance could be negatively impacted by changes in tax laws or regulations.

We and our customers are subject to a wide variety of tax laws and regulations in jurisdictions around the world. In response to recent economic challenges, we anticipate that many of the jurisdictions in which we and our customers do business will review tax and other revenue raising laws and regulations. New income, sales, use or other tax laws, statutes, rules, regulations or ordinances could be enacted at any time. Further, existing tax laws, statutes, rules, regulations or ordinances could be interpreted, changed, modified or applied adversely to us or our customers. Any changes to these existing tax laws could adversely affect our domestic and international business operations, and our business and financial performance. Additionally, these events could require us or our customers to pay additional tax amounts on a prospective or retroactive basis, as well as require us or our customers to pay fines and/or penalties and interest for past amounts deemed to be due. Additionally, new, changed, modified or newly interpreted or applied tax laws could increase our customers' and our compliance, operating and other costs, as well as the costs of our products. Further, these events could decrease the capital we have available to operate our business. Any or all of these events could adversely impact our business and financial performance.

We have recorded a significant deferred tax asset, and we might never realize the full value of our deferred tax asset, which would result in a charge against our earnings.

In connection with the initial acquisition of our common stock as part of our recapitalization in 1999, we recorded approximately \$107.0 million as a deferred tax asset. As of December 31, 2013, we have deferred tax assets recognized of \$60.1 million, of which \$5.8 million relates to our 1999 recapitalization.

Realization of our deferred tax asset is dependent upon our generating sufficient taxable income in future years to realize the tax benefit from that asset. Deferred tax assets are reviewed at least annually for realizability. A charge against our earnings would result if, based on the available evidence, it is more likely than not that some portion of the deferred tax asset will not be realized. This could be caused by, among other things, deterioration in performance, loss of key contracts, adverse market conditions, adverse changes in applicable laws or regulations, including changes that restrict the activities of or affect the products sold by our business and a variety of other factors. If a deferred tax asset

was determined to be not realizable in a future period, the charge to earnings would be recognized as an expense in our results of operations in the period the determination is made. Additionally, if we are unable to utilize our deferred tax assets, our cash flow available to fund operations could be adversely effected.

Depending on future circumstances, it is possible that we might never realize the full value of our deferred tax asset. Any future determination of impairment of a significant portion of our deferred tax asset would have an adverse effect on our financial condition and results of operations.

Our ability to utilize our net operating loss carryforwards may be limited.

Included in our deferred tax asset balance is \$14.6 million related to federal net operating loss carryforwards at December 31, 2013. Our federal net operating loss carryforwards are subject to limitations on how much may be utilized on an annual basis. The use of the net operating loss carryforwards may have additional limitations resulting from certain future ownership changes or other factors set forth in the Internal Revenue Code. If our net operating loss carryforwards are further limited, and we have taxable income which exceeds the available net operating loss carryforwards for that period, we would incur an income tax liability even though net operating loss carryforwards may be available in future years prior to their expiration, which would have an adverse effect on our future cash flow, financial condition and results of operations.

We might face challenges in integrating acquisitions and, as a result, might not realize the expected benefits of these acquisitions.

We have completed significant acquisitions over the past five years and we may undertake additional acquisitions in the future. Managing and integrating the operations and personnel of an acquired company can be a complex process. The integration might not be completed rapidly or achieve the anticipated benefits of the acquisition. The successful integration of acquired companies will require, among other things, coordination of various departments, including product development, engineering, sales and marketing and finance. Further, a successful integration of acquired companies internal control structure will be required. The diversion of the attention of management and any difficulties encountered in this process could cause the disruption of, or a loss of momentum in, sales or product development. If we are unable to successfully integrate the operations and personnel of our recently acquired companies, or if there is any significant delay in achieving integration, we will not realize the revenue growth, synergies and other anticipated benefits we expected and our business and results of operations could be adversely affected.

If we are unable to retain key personnel of our acquisitions, our business may suffer.

The success of our acquisitions will depend in part on our ability to retain their engineering, sales, marketing, development and other personnel. It is possible that these employees might decide to terminate their employment. If key employees terminate their employment, the sales, marketing or development activities of acquired companies might be adversely affected, our management's attention might be diverted from successfully integrating the acquired operations and to hiring suitable replacements and, as a result, our business might suffer.

Future acquisitions could prove difficult to integrate, disrupt our business, dilute stockholder value and strain our resources.

As part of our business strategy, we have made acquisitions in the past, and, we might acquire additional companies, services and technologies that we feel could complement or expand our business, augment our market coverage, enhance our technical capabilities, provide us with important customer contacts or otherwise offer growth opportunities. Acquisitions and investments involve numerous risks, including:

- Difficulties in integrating operations, technologies, services, accounting and personnel;
- Difficulties in supporting and transitioning customers of our acquired companies;
- Diversion of financial and management resources from existing operations;
- Risks of entering new sectors of the nonprofit industry;
- Potential loss of key employees; and
- Inability to generate sufficient return on investment.

Acquisitions also frequently result in recording of goodwill and other intangible assets, which are subject to potential impairments in the future that could harm our operating results. In addition, if we finance acquisitions by issuing equity securities or securities convertible into equity securities, our existing stockholders would be diluted which, in turn, could affect the market price of our stock. Moreover, we could finance any acquisition with debt, resulting in higher leverage and interest costs. As a result, if we fail to evaluate and execute acquisitions or investments properly, we might not achieve the anticipated benefits of any such acquisition and we may incur costs in excess of what we

anticipate. Furthermore, if we incur additional

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debt to fund acquisitions and are unable to service our debt obligation we may have a greater risk of default under our credit facility.

If we are not able to manage our anticipated growth effectively, our operating costs may increase and our operating margins may decrease.

We will need to continue to grow our infrastructure to address our acquisitions and other potential market opportunities. Our growth will continue to place, to the extent that we are able to sustain such growth, a strain on our management, administrative, operational and financial infrastructure. If we continue to grow our operations, by way of additional business combinations or otherwise, we may not be effective in enlarging our physical facilities and our systems and our procedures or controls may not be adequate to support such expansion or our business generally. If we are unable to manage our growth, our operating costs may increase and our operating margins may decrease.

Increasing government regulation could affect our business.

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

• User privacy;

• Payment processing;

• The pricing and taxation of goods and services offered over the Internet;

• Taxation of foreign earnings;

• The content of websites;

• Copyrights;

• Consumer protection, including the potential application of “do not call” registry requirements on our customers and consumer backlash in general to direct marketing efforts of our customers;

• The online distribution of specific material or content over the Internet; and

• The characteristics and quality of products and services offered over the Internet.

Pending and enacted legislation at the state and federal levels, including those related to fundraising activities, may also restrict further our information gathering and disclosure practices, for example, by requiring us to comply with extensive and costly registration, reporting or disclosure requirements.

Item 1B. Unresolved staff comments

None.

Item 2. Properties

We lease our headquarters in Charleston, South Carolina which consists of approximately 220,000 square feet. The lease on our Charleston headquarters expires in October 2024, and we have the option for two 5-year renewal periods. We also lease additional facilities in Charleston, South Carolina; Austin, Texas; Indianapolis, Indiana, Cambridge, Massachusetts; Washington D.C.; San Diego and Emeryville, California; Overland Park, Kansas; Lincoln, Nebraska; Miami, Florida; Almere, the Netherlands; Glasgow, Scotland; Dublin, Ireland; London, England; East Brisbane, Australia; and Sydney, Australia. We believe that our properties are in good operating condition and adequately serve our current business operations for all of our business segments. We also anticipate that suitable additional or alternative space, including those under lease options, will be available at commercially reasonable terms for future expansion.

Item 3. Legal proceedings

From time to time we may become involved in litigation relating to claims arising from our ordinary course of business. We do not believe that there are any claims or actions pending or threatened against us, the ultimate disposition of which would have a material adverse effect on us.

Item 4. Mine safety disclosures
Not applicable.

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PART II

Item 5. Market for registration's common equity, related stockholder matters and issuer purchases of equity securities
 Our common stock began trading on the NASDAQ National Market under the symbol "BLKB" on July 26, 2004. On July 1, 2006, our common stock began trading on NASDAQ's newest market tier, the NASDAQ Global Select Market. The following table sets forth the high and low sales prices for shares of our common stock, as reported by NASDAQ for the periods indicated.

Blackbaud quarterly high and low stock prices

	High	Low
Fiscal year ended December 31, 2013		
First quarter	\$30.84	\$22.85
Second quarter	\$34.44	\$27.68
Third quarter	\$40.00	\$32.54
Fourth quarter	\$42.23	\$33.88
Fiscal year ended December 31, 2012		
First quarter	\$34.00	\$22.63
Second quarter	\$33.93	\$24.02
Third quarter	\$28.34	\$22.98
Fourth quarter	\$24.88	\$20.99

As of February 12, 2014, there were approximately 156 stockholders of record of our common stock. Because many of our shares of common stock are held by brokers and other institutions on behalf of stockholders, this number is not representative of the total number of stockholders represented by these stockholders of record. On February 12, 2014, the closing price of our common stock was \$32.56.

Stock performance graph

The following performance graph shall not be deemed to be “soliciting material” or “filed” or incorporated by reference in future filings with the SEC, or subject to the liabilities of Section 18 of the Exchange Act except as shall be expressly set forth by specific reference in such filing. The performance graph compares the performance of our common stock to the NASDAQ Composite Index and the NASDAQ Computer and Data Processing Index. The graph covers the most recent five-year period ending December 31, 2013. The graph assumes that the value of the investment in our common stock and each index was \$100.00 at December 31, 2008, and that all dividends are reinvested.

	12/31/2008	12/31/2009	12/31/2010	12/31/2011	12/31/2012	12/31/2013
Blackbaud, Inc.	\$ 100.00	\$ 179.61	\$ 200.64	\$ 218.64	\$ 183.59	\$ 307.39
NASDAQ Composite	\$ 100.00	\$ 144.88	\$ 170.58	\$ 171.30	\$ 199.99	\$ 283.39
NASDAQ Computer & Data Processing	\$ 100.00	\$ 165.29	\$ 179.77	\$ 177.69	\$ 191.22	\$ 290.35

Common stock acquisitions and repurchases

The following table provides information about shares of common stock acquired or repurchased during the three months ended December 31, 2013. All of these acquisitions were of common stock withheld by us to satisfy minimum tax obligations of employees due upon vesting of restricted stock awards and units and exercise of stock appreciation rights.

Period	Total number of shares acquired or purchased	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 plan or programs (in thousands)
Beginning balance, October 1, 2013				\$50,000
October 1, 2013 through October 31, 2013	6,187	\$40.52	—	\$50,000
November 1, 2013 through November 30, 2013	141,615	\$35.56	—	\$50,000
December 1, 2013 through December 31, 2013	23	\$36.97	—	\$50,000
Total	147,825	\$35.77	—	\$50,000

In August 2010, our Board of Directors approved a stock repurchase program that authorized us to purchase up to (1) \$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.

Dividend policy and restrictions

Our Board of Directors has adopted a dividend policy which reflects an intention to distribute to our stockholders a portion of the cash generated by our business that exceeds our operating needs and capital expenditures as regular quarterly dividends. This policy reflects our judgment that we can provide greater value to our stockholders by distributing to them a portion of the cash generated by our business.

In accordance with this dividend policy, we paid quarterly dividends at an annual rate of \$0.48 per share in 2013 and 2012, resulting in an aggregate dividend payment to stockholders of \$22.1 million and \$21.7 million in 2013 and 2012, respectively. In February 2014, our Board of Directors approved an annual dividend rate of \$0.48 per share for 2014. We declared a first quarter dividend of \$0.12 per share payable on March 14, 2014, to stockholders of record on February 28, 2014, and currently intend to pay quarterly dividends at an annual rate of \$0.48 per share of common stock for each of the remaining fiscal quarters in 2014. Dividends at this rate would total approximately \$22.6 million in the aggregate on the common stock in 2014 (assuming 47.0 million shares of common stock are outstanding, net of treasury stock).

Dividends on our common stock will not be cumulative. Consequently, if dividends on our common stock are not declared and/or paid at the targeted level, our stockholders will not be entitled to receive such payments in the future. We are not obligated to pay dividends, and as described more fully below, our stockholders might not receive any dividends as a result of the following factors:

- Our credit facility limits the amount of dividends we are permitted to pay;
- Our Board of Directors could decide to reduce dividends or not to pay dividends at all, at any time and for any reason;
 - The amount of dividends distributed is subject to state law restrictions;
 - and

- We might not have enough cash to pay dividends due to changes to our operating earnings, working capital requirements and anticipated cash needs.

Assumptions and considerations

We estimate that the cash necessary to fund dividends on our common stock for 2014 at an annual rate of \$0.48 per share is approximately \$22.6 million (assuming 47.0 million shares of common stock are outstanding, net of treasury stock).

We have a stock repurchase program that authorizes us to purchase up to \$50.0 million of our outstanding shares of common stock. The program does not have an expiration date. The shares could be purchased in a self-tender for our stock, from time to time on the open market or in privately negotiated transactions depending upon market conditions and other factors, all in accordance with the requirements of applicable law. Any open market purchases under the repurchase program will be made in compliance with Rule 10b-18 of the Securities Exchange Act of 1934 and all other applicable securities regulations. We might not purchase any shares of common stock and our Board of Directors may decide, in its absolute discretion, at any time and for any reason, to cancel the stock repurchase program.

We believe that our cash on hand and the cash flows we expect to generate from operations will be sufficient to meet our liquidity requirements through 2014, including dividends and purchases under our stock repurchase program. See “Management’s discussion and analysis of financial conditions and results of operations — Liquidity and capital resources” in this report.

If our assumptions as to operating expenses, working capital requirements and capital expenditures are too low or if unexpected cash needs arise that we are not able to fund with cash on hand or with borrowings under our credit facility, we would need to either reduce or eliminate dividends. If we were to use working capital or permanent borrowings to fund dividends, we would have less cash available for future dividends and other purposes, which could negatively impact our stock price, financial condition, results of operations and ability to maintain or expand our business.

We have estimated our dividend only for 2014, and we cannot assure our stockholders that during or following 2014 we will pay dividends at the estimated levels, or at all. We are not required to pay dividends and our Board of Directors may modify or revoke our dividend policy at any time. Dividend payments are within the absolute discretion of our Board of Directors and will be dependent upon many factors and future developments that could differ materially from our current expectations. Indeed, over time our capital and other cash needs, including unexpected cash needs, will invariably change and remain subject to uncertainties, which could impact the level of any dividends we pay in the future.

We believe that our dividend policy could limit, but not preclude, our ability to pursue growth as we intend to retain sufficient cash after the distribution of dividends to permit the pursuit of growth opportunities that do not require material capital investments. In order to pay dividends at the level currently anticipated under our dividend policy and to fund any substantial portion of our stock repurchase program, we expect that we could require financing or borrowings to fund any significant acquisitions or to pursue growth opportunities requiring capital expenditures significantly beyond our anticipated capital expenditure levels. Management will evaluate potential growth opportunities as they arise and, if our Board of Directors determines that it is in our best interest to use cash that would otherwise be available for distribution as dividends to pursue an acquisition opportunity, to materially increase capital spending or for some other purpose, the Board would be free to depart from or change our dividend policy at any time.

Restrictions on payment of dividends

Under Delaware law, we can only pay dividends either out of “surplus” (which is defined as total assets at fair market value minus total liabilities, minus statutory capital) or out of current or the immediately preceding year’s earnings. As of December 31, 2013, we had \$11.9 million in cash and cash equivalents. In addition, we anticipate that we will have sufficient earnings in 2014 to pay dividends at the level described above. Although we believe we will have sufficient surplus and earnings to pay dividends at the anticipated levels for 2014, our Board of Directors will seek periodically to assure itself of this sufficiency before actually declaring any dividends.

We entered into an amended and restated credit facility in February 2012. The amended credit facility restricts our ability to declare and pay dividends on our common stock. In order to pay any cash dividends and/or repurchase shares of stock: (1) no default or event of default shall have occurred and be continuing under the credit facility, and (2) we must be in compliance with a leverage ratio set forth in the credit agreement. See “Management’s discussion and analysis of financial conditions and results of operations — Liquidity and capital resources” in this report.

Item 6. Selected financial data

The selected financial data set forth below should be read in conjunction with “Management’s discussion and analysis of financial condition and results of operations” and our financial statements and the related notes included elsewhere in this report to fully understand factors that may affect the comparability of the information presented below.

The following data, insofar as it relates to each of the years ended December 31, 2013, 2012 and 2011, has been derived from the audited annual financial statements, including the consolidated balance sheets at December 31, 2013 and 2012, and the related consolidated statements of comprehensive income, cash flows and stockholders’ equity for the three years ended December 31, 2013, 2012 and 2011 and notes thereto appearing elsewhere herein. The following data, insofar as it relates to each of the years ended December 31, 2010 and 2009, and the consolidated balance sheets as of December 31, 2011, 2010 and 2009 are derived from audited financial statements not included in this report.

As described in Note 3 of the consolidated financial statements included in this annual report, our business acquisitions could affect the comparability of the information presented.

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(in thousands, except per share data)	Year ended December 31,				
	2013	2012	2011	2010	2009
Consolidated statements of comprehensive income data:					
Revenue					
License fees	\$16,715	\$20,551	\$19,475	\$23,719	\$25,656
Subscriptions	212,656	162,102	103,544	83,912	73,194
Services	126,548	119,626	108,781	87,663	87,239
Maintenance	138,745	136,101	130,604	124,559	116,413
Other revenue	9,153	9,039	8,464	6,712	6,968
Total revenue	503,817	447,419	370,868	326,565	309,470
Cost of revenue					
Cost of license fees	2,763	2,993	3,345	3,003	3,697
Cost of subscriptions ⁽¹⁾	93,649	68,773	42,536	31,155	28,158
Cost of services ⁽¹⁾	104,005	97,208	79,086	66,755	61,585
Cost of maintenance ⁽¹⁾	25,741	26,001	25,178	24,123	21,594
Cost of other revenue	6,505	7,485	7,049	7,103	6,098
Total cost of revenue	232,663	202,460	157,194	132,139	121,132
Gross profit	271,154	244,959	213,674	194,426	188,338
Operating expenses					
Sales and marketing ⁽¹⁾	97,614	95,218	75,361	69,469	63,495
Research and development ⁽¹⁾	65,645	64,692	47,672	45,499	45,520
General and administrative ⁽¹⁾	50,320	63,133	36,933	32,636	33,383
Restructuring	3,494	175	—	—	—
Amortization	2,539	2,106	980	798	768
Impairment of cost method investment	—	200	1,800	—	—
Total operating expenses	219,612	225,524	162,746	148,402	143,166
Income from operations	51,542	19,435	50,928	46,024	45,172
Interest income	67	146	183	84	637
Interest expense	(5,818)	(5,864)	(200)	(74)	(962)
Other income (expense), net	(462)	(392)	346	(98)	220
Income before provision for income taxes	45,329	13,325	51,257	45,936	45,067
Income tax provision	14,857	6,742	18,037	16,749	17,547
Net income	\$30,472	\$6,583	\$33,220	\$29,187	\$27,520
Earnings per share					
Basic	\$0.68	\$0.15	\$0.76	\$0.68	\$0.64
Diluted	\$0.67	\$0.15	\$0.75	\$0.67	\$0.63
Common shares and equivalents outstanding					
Basic weighted average shares	44,685	44,146	43,523	43,145	42,771
Diluted weighted average shares	45,421	44,692	44,149	43,876	43,600
Dividends per share	\$0.48	\$0.48	\$0.48	\$0.44	\$0.40
Summary of stock-based compensation:					
Cost of subscriptions	\$1,032	\$860	\$571	\$392	\$387
Cost of services	2,464	2,786	1,966	1,742	1,433
Cost of maintenance	545	538	741	814	750
Total included in cost of revenue	4,041	4,184	3,278	2,948	2,570
Sales and marketing	2,351	2,527	1,325	1,366	1,605
Research and development	3,731	3,556	3,039	2,844	2,944
General and administrative	6,787	8,973	7,242	5,901	5,291

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Total included in operating expenses	12,869	15,056	11,606	10,111	9,840
Total stock-based compensation	\$16,910	\$19,240	\$14,884	\$13,059	\$12,410

(1) Includes stock-based compensation as set forth in tabular summary of stock-based compensation for all periods presented.

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(in thousands)	December 31,				
	2013	2012	2011	2010	2009
Consolidated balance sheet data					
Cash and cash equivalents	\$ 11,889	\$ 13,491	\$ 52,520	\$ 28,004	\$ 22,769
Deferred tax asset, including current portion	13,629	15,799	30,927	47,478	59,284
Working (deficit) capital	(126,913)	(97,947)	(52,093)	(57,056)	(74,458)
Total assets	706,610	705,747	392,590	323,806	299,927
Deferred revenue, including current portion	190,574	185,018	163,437	150,661	137,950
Total long-term liabilities	188,384	246,368	12,547	9,319	7,891
Common stock	56	55	54	53	52
Additional paid-in capital	220,763	203,638	175,401	158,372	134,643
Total stockholders' equity	\$ 161,544	\$ 147,684	\$ 140,002	\$ 116,469	\$ 110,293

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Blackbaud, Inc.

Item 7. 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 Item 1A Risk factors and our consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K. 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 "Item 1A. Risk factors" 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 cloud-based and on-premise software solutions and related services designed specifically for nonprofit organizations. Our products and services enable nonprofit organizations to increase donations, reduce fundraising costs, improve communications with constituents, manage their finances and optimize internal operations. We continue to make investments in our product portfolio and go-to-market organization to ensure we are properly positioned to benefit from shifts in the market, including demand for our subscription-based offerings. As of December 31, 2013, we had more than 29,000 active customers distributed across multiple verticals within the nonprofit market including education, foundations, health and human services, religion, arts and cultural, public and societal benefits, environment and animal welfare as well as international foreign affairs.

We derive revenue from charging subscription fees for the use of our SaaS 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. Consulting, training and implementation are generally not essential to the functionality of our software products and are sold separately. Furthermore, we derive revenue from providing hosting services, performing donor prospect research engagements, selling lists of potential donors, and providing transaction processing services, benchmarking studies and data modeling services.

We completed our acquisition of Convio in May 2012 for \$335.7 million in consideration. We have included the results of operations of Convio in our consolidated results of operations from the date of acquisition, which impacts the comparability of our statements of comprehensive income when comparing 2013 to 2012 and 2012 to 2011. Because we have integrated a substantial amount of the Convio operations and have made product rationalization decisions, it is not possible to determine the revenue and operating costs attributable solely to the acquired business for 2013.

Overall, revenue in 2013 increased \$56.4 million or 13% when compared to 2012. This increase was primarily the result of the inclusion of Convio for the full year in 2013 compared to only eight months in 2012 as well as growth in demand for our online and hosted solutions, as our business continues to shift towards subscription-based offerings. An increase in the volume of transactions for which we process payments also contributed to the increase in subscription revenue as well as a change in presentation from net to gross for revenues and costs associated with certain of our payment processing services effective October 2013.

Income from operations for 2013 increased by \$32.1 million or 165% when compared to 2012. The increase in income from operations was primarily attributable to a reduction in costs from improved operational efficiencies realized as we integrated Convio's operations and a reduction in acquisition related costs. Also contributing to the increase was the inclusion of Convio's subscription-based offerings, which have historically yielded higher gross margins than our historical subscription-based offerings and an increase in demand for our online fundraising offerings and our payment processing services, which have historically yielded higher gross margins than our other offerings. These favorable impacts on income from operations were partially offset by an increase in amortization of acquired intangibles.

At December 31, 2013, our cash and cash equivalents were \$11.9 million and outstanding borrowings were \$152.9 million. During 2013, we generated \$107.2 million in cash flow from operations, paid \$22.1 million in dividends, used \$20.1 million to purchase computer equipment and software and reduced our debt balance by \$62.6 million. During 2013, we continued to experience growth in overall revenue primarily driven by the inclusion of Convio's product offerings and the growing demand for our subscription-based offerings. We plan to further increase our focus on subscription-based offerings as we execute on our key growth initiatives and strengthen our leadership position, while achieving our targeted level of profitability. In the near term, we anticipate there will continue to be a dilutive impact on our profitability as we invest

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Blackbaud, Inc.

Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

in our product portfolio to meet demand for our subscription offerings and shift from a perpetual license-based model, with upfront revenue recognition, to a subscription-based model, with recognition of revenue occurring ratably over the subscription term.

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

Results of operations

During 2013, 2012 and 2011, we acquired companies that provided us with strategic opportunities to expand our share of the nonprofit market through the integration of complementary products and services to serve the changing needs of our customers. The following are the companies we acquired and their respective acquisition date:

Public Interest Data, Inc., or PIDI – February 1, 2011;

Everyday Hero Pty. Ltd., or EDH – October 6, 2011;

Convio, Inc., or Convio – May 4, 2012; and

MyCharity, Ltd. – March 6, 2013

We have included the results of operations of acquired companies in our consolidated statements of comprehensive income from the date of their respective acquisition, which impacts the comparability of our results of operations when comparing 2013 to 2012 and 2012 to 2011. Because we have integrated a substantial amount of these operations, it is impracticable to determine the operating costs attributable solely to the acquired businesses for 2013. We have noted in the discussion below, to the extent meaningful, the impact on the comparability of our consolidated statements of comprehensive income due to the inclusion of acquired companies.

Comparison of the years ended December 31, 2013 and 2012**Revenue by segment**

The table below compares revenue by segment for year ended December 31, 2013, with the same period in 2012.

(in millions)	Year ended December 31,				
	2013	2012	Change	% Change	
ECBU	\$195.6	\$165.1	\$30.5	18	%
GMBU	225.3	203.2	22.1	11	%
IBU	41.5	40.1	1.4	3	%
Target Analytics	39.8	37.5	2.3	6	%
Other	1.6	1.5	0.1	7	%
Total revenue	\$503.8	\$447.4	\$56.4	13	%

The increases in revenue for ECBU and GMBU during 2013 when compared to 2012 were primarily attributable to growth in subscriptions revenue as a result of the inclusion of Luminare Online, previously a Convio product, and an increase in the volume of transactions for which we process payments. Also contributing to the growth in ECBU revenue were increases in revenue from consulting services and our Blackbaud CRM hosting services. Also contributing to the growth in GMBU revenue was the continued increase in demand for our online and hosted solutions as our business shifts towards subscription-based offerings.

IBU revenue increased during 2013 when compared to 2012 primarily due to incremental subscriptions revenue. The growth in IBU subscriptions revenue was primarily attributable to an increase in variable transaction revenue associated with the use of our products to fundraise online. Also contributing to the increase in IBU subscriptions revenue was an increase in demand for our online and hosted fundraising solutions including Everyday Hero, the Raiser's Edge and eTapestry.

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Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

Target Analytics revenue growth during 2013 when compared to 2012 was primarily the result of an increase in demand for our prospect research offerings. Also contributing to the increase in Target Analytics revenue was growth in our performance management and data enrichment portfolios, driven by improved sales execution.

Included in ECBU, GMBU and IBU revenue for 2013 is \$3.3 million, \$5.0 million and \$0.2 million, respectively, attributable to a prospective change in presentation from net to gross for revenue and costs associated with our payment processing services as a result of certain third-party arrangements that had changes in contractual terms effective October 2013.

Operating results

License fees

(in millions)	Year ended December 31,			
	2013	2012	Change	% Change
License fees revenue	\$ 16.7	\$ 20.6	\$(3.9)	(19)%
Cost of license fees	2.8	3.0	(0.2)	(7)%
License fees gross profit	\$ 13.9	\$ 17.6	\$(3.7)	(21)%
License fees gross margin	83	% 85	%	

We derive license fees revenue from the sale of our software products under a perpetual license agreement.

During 2013, revenue from license fees decreased primarily as a result of smaller contributions of revenue from our Raiser's Edge and Financial Edge offerings when compared to 2012. In addition, we continue to meet the demand of our emerging and mid-sized customers that increasingly prefer subscription-based hosted applications instead of solutions offered under traditional on-premise perpetual license arrangements. Also contributing to the decreases in revenue from license fees was a prospective change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January 2013. The net revenue attributable to these third-party software arrangements has been included in "Other revenue" for 2013.

Cost of license fees is primarily comprised of third-party software royalties, variable reseller commissions, amortization of software development costs and amortization of intangibles from business combinations. The decrease in cost of license fees during 2013 when compared to 2012 was primarily due to a decrease in third-party software royalties resulting from a prospective change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January 2013.

The decrease in license fees gross margin during 2013 when compared to 2012 was primarily due to the decrease in license fees revenue combined with more sales of products that have third-party software royalty costs associated with them.

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Blackbaud, Inc.

Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

Subscriptions

(in millions)	Year ended December 31,				
	2013	2012	Change	% Change	
Subscriptions revenue	\$212.7	\$162.1	\$50.6	31	%
Cost of subscriptions	93.7	68.8	24.9	36	%
Subscriptions gross profit	\$119.0	\$93.3	\$25.7	28	%
Subscriptions gross margin	56	% 58	%		

Revenue from subscriptions is primarily comprised of revenue from charging for the use of our software products, which includes providing access to hosted applications and hosting services, access to certain data services and our online subscription training offerings, as well as revenue from variable transaction fees associated with the use of our products to fundraise online. We continue to experience growth in sales of our hosted applications and hosting services as we meet the demand of our emerging and mid-sized customers that increasingly prefer subscription-based offerings.

The increase in subscriptions revenue was primarily attributable to the inclusion of Convio for the full year in 2013 compared to only eight months in 2012, and an increase in demand for our online fundraising offerings. Also contributing to the growth in subscriptions revenue was an increase in the volume of transactions for which we process payments as well as an \$8.5 million increase attributable to a prospective change in presentation from net to gross for revenues and costs associated with certain of our payment processing services effective October 2013. 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 software development costs, amortization of intangibles from business combinations and other costs incurred in providing support and services to our customers. The increase in cost of subscriptions during 2013 when compared to 2012 was primarily attributable to increases in amortization of intangibles from business combinations, hosting costs, human resource costs and allocated depreciation, facilities and IT support costs. The increase also included \$8.5 million of costs attributable to a prospective change in presentation from net to gross for revenues and costs associated with certain of our payment processing services effective October 2013.

Amortization of intangibles from business combinations increased by \$6.6 million during 2013 when compared to 2012 primarily due to the acquisition of Convio and the inclusion of a full year of intangibles amortization in 2013 compared to only eight months in 2012.

Hosting costs, human resource costs and allocated depreciation, facilities and IT support costs increased by \$3.2 million, \$3.1 million and \$2.8 million, respectively, during 2013 when compared to 2012. These increases were primarily a result of the inclusion of Convio and investments made to support anticipated growth in our subscription-based offerings.

Subscriptions gross margin decreased during 2013 when compared to 2012 primarily as a result of the cost increase from the prospective change in presentation from net to gross revenues and costs as discussed above and non-cash amortization of intangible assets purchased. Excluding the effect of the change in presentation, gross margin was relatively unchanged from 2012.

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Blackbaud, Inc.

Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

Services

(in millions)	Year ended December 31,			
	2013	2012	Change	% Change
Services revenue	\$126.5	\$119.6	\$6.9	6 %
Cost of services	104.0	97.2	6.8	7 %
Services gross profit	\$22.5	\$22.4	\$0.1	— %
Services gross margin	18	% 19	%	

We derive services revenue from consulting, installation, implementation, education and analytic services. Consulting, installation and implementation services involve converting data from a customer's existing system, assistance in file set up and system configuration, and/or process re-engineering. 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 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. We typically recognize services revenue upon delivery. We also recognize certain direct and incremental costs associated with consulting services revenue as that revenue is earned. We recognize revenue from upfront activation fees ratably over the estimated period the customer benefits from those upfront services. We continue to expense indirect costs in the period the services are provided.

The increase in services revenue during 2013 when compared to 2012 was attributable to increases in consulting, education and analytic services revenue of \$4.1 million, \$1.8 million and \$1.0 million, respectively. Consulting services revenue increased primarily due to the inclusion of Convio for the full year in 2013 compared to only eight months in 2012. The volume of education services revenue increased due to higher demand for our subscription-based training. Analytic services revenue increased primarily due to an increase in demand for our prospect research offerings. Also contributing to the increase in analytic services revenue was growth in our performance management and data enrichment portfolios, driven by improved sales execution.

Cost of services is primarily comprised of human resource costs, stock-based compensation expense, third-party contractor expenses, 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. The increase in cost of services during 2013 when compared to 2012 was primarily attributable to increases in human resource costs, the recognition of deferred implementation service costs and allocated depreciation, facilities and IT support costs. Human resource costs increased \$3.8 million primarily as a result of increases in accrued bonus costs, merit-based salary increases and employee health care costs. Our recognition of implementation service costs increased \$2.2 million during 2013 when compared to 2012 due to a decrease in the amount of costs that are being deferred in connection with our shift from traditional license and related service arrangements to subscription offerings. Allocated depreciation, facilities and IT support costs increased \$0.8 million due to the inclusion of allocable costs from the Convio operations as well as investments we have made in our infrastructure to make our operations more scalable.

Services gross margin decreased in 2013 when compared to 2012 primarily due to increases in human resource costs and allocated costs outpacing the growth of services revenue. Also contributing to the decrease in services gross margin was the inclusion of Convio's service offerings for a full year in 2013, which have historically yielded lower gross margins. Since our acquisition of Convio in May 2012, we have made significant progress integrating operations and realizing gross margin synergies from the combination. However, the impact on services gross margin is obscured by the inclusion of Convio operating results for the full year in 2013 compared to only eight months in 2012.

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Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

Maintenance

(in millions)	Year ended December 31,			
	2013	2012	Change	% Change
Maintenance revenue	\$138.7	\$136.1	\$2.6	2 %
Cost of maintenance	25.7	26.0	(0.3)	(1)%
Maintenance gross profit	\$113.0	\$110.1	\$2.9	3 %
Maintenance gross margin	81	% 81	%	

Revenue from maintenance 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 periods reported did not vary materially compared to prior periods.

The increase in maintenance revenue during 2013 when compared to 2012 was primarily comprised of (i) \$10.9 million of incremental maintenance from new customers associated with new license agreements and increases in contracts with existing customers; and (ii) approximately \$4.2 million of incremental maintenance from contract inflationary rate adjustments; partially offset by (iii) a \$8.4 million reduction in maintenance from contracts that were not renewed and reductions in contracts with existing customers; and (iv) \$3.3 million decrease in maintenance revenue attributable to a prospective change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January 2013. The net revenue attributable to these third-party software arrangements has been included in "Other revenue" for 2013. 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 decreased during 2013 when compared to 2012 primarily due to a decrease in proprietary software costs, partially offset by increases in human resource costs and allocated depreciation, facilities and IT support costs. The decrease in proprietary software costs was primarily attributable to a prospective change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January 2013. The increase in human resource costs was primarily due to merit-based salary increases and an increase in employee health care costs.

Maintenance gross margin in 2013 remained relatively unchanged when compared 2012.

Other revenue

(in millions)	Year ended December 31,			
	2013	2012	Change	% Change
Other revenue	\$9.2	\$9.0	\$0.2	2 %
Cost of other revenue	6.5	7.5	(1.0)	(13)%
Other gross profit	\$2.7	\$1.5	\$1.2	80 %
Other gross margin	29	% 17	%	

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

Other revenue increased during 2013 when compared to 2012 primarily due to a \$1.5 million increase in third-party software referral revenue upon the prospective change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January

2013. During 2012, revenue from these arrangements was recorded on a gross basis to license fees, subscription and maintenance. The increase in third-party

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Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

software referral fees during 2013 when compared to 2012 was partially offset by a decrease in revenue from reimbursement of travel-related expenses associated with services revenue.

Cost of other revenue includes 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. Cost of other revenue decreased during 2013 when compared to 2012 primarily due to fewer reimbursable expenses related to services provided at customer locations. Other revenue gross margin increased in 2013 when compared to 2012 primarily due to an increase in third-party software referral fees attributable to the prospective change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January 2013.

Operating expenses

Sales and marketing

(in millions)	Year ended December 31,				
	2013	2012	Change	% Change	
Sales and marketing expense	\$97.6	\$95.2	\$2.4	3	%
% of revenue	19	% 21	%		

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 2013 when compared to 2012 primarily due to a \$1.1 million increase in sales commissions, a \$0.9 million increase in allocated depreciation, facilities and IT support costs and a \$0.8 million increase in human resource costs. The increase in sales commissions is primarily due to an increased amount of commissionable revenue from 2012 to 2013. The increase in allocated depreciation, facilities and IT support costs resulted from both the inclusion of allocable costs from the Convio operations as well as investments we have made in our infrastructure to make our operations more scalable. The increase in human resource costs was primarily due to increases in employee health care costs and accrued bonus costs, partially offset by a reduction in headcount in connection with the realignment of our workforce, which began in January 2013.

Since the acquisition of Convio in May 2012, we have made significant progress integrating operations and realizing cost synergies from the combination, which is reflected in the improvements in sales and marketing expense as a percentage of revenue for 2012 to 2013.

Research and development

(in millions)	Year ended December 31,				
	2013	2012	Change	% Change	
Research and development expense	\$65.6	\$64.7	\$0.9	1	%
% of revenue	13	% 14	%		

We have made substantial investments in research and development and expect to continue to do so as a part of our strategy to introduce additional products and services. Research and development expense includes human resource costs, stock-based compensation expense, third-party contractor expenses, software development tools and certain other expenses related to researching and developing new products, and allocated depreciation, facilities and IT support costs.

Research and development expense increased during 2013 when compared to 2012 primarily due to a \$1.5 million increase in human resource costs and a \$1.7 million increase in allocated depreciation, facilities and IT support costs, partially offset by a \$2.0 million increase in the amount of software development costs that were capitalized. Human resource costs increased primarily due to the inclusion of additional headcount from Convio. The increase in allocated depreciation, facilities and IT

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Blackbaud, Inc.

Item 7. Management's discussion and analysis of financial condition and results of operations (continued)

support costs resulted from both the inclusion of allocable costs from the Convio operations as well as investments we have made in our infrastructure to make our operations more scalable. We expect incremental research and development expense in 2014 as we continue to invest in product enhancement and new product innovation.

Since the acquisition of Convio in May 2012, we have made significant progress integrating operations and realizing cost synergies from the combination, which is reflected in the improvement in research and development expense as a percentage of revenue from 2012 to 2013.

General and administrative

(in millions)	Year ended December 31,			
	2013	2012	Change	% Change
General and administrative expense	\$50.3	\$63.1	\$(12.8)	(20)%
% of revenue	10	% 14	%	

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 decreased during 2013 when compared to 2012 primarily due to decreases in acquisition-related costs and stock-based compensation as well as an increase in the amount of costs allocated out of general and administrative expense including depreciation, IT support costs and certain facilities costs. These reductions in general and administrative expense were partially offset by increases in facilities costs, human resource costs and costs associated with the replacement of our CEO. Acquisition-related costs associated with our acquisition of Convio decreased \$13.1 million during 2013 when compared to 2012. Stock-based compensation decreased \$2.2 million during 2013 when compared to 2012 primarily due to the departure of employees in connection with the realignment of our workforce, which began in January 2013, and the departure of certain executive officers, including our CEO during 2013. Business costs allocated out of general and administrative expense increased \$5.6 million during 2013 when compared to 2012 primarily due to the inclusion of Convio's operations for the full year in 2013 compared to only eight months in 2012. Facilities costs increased by \$3.9 million primarily due to the inclusion of Convio's operations for the full year in 2013 compared to only eight months in 2012. Human resource costs increased \$3.3 million during 2013 when compared to 2012 primarily due to additional resources needed to support the growth of our business. We also incurred \$2.4 million of incremental costs during 2013 when compared to 2012 associated with severance provided to our former CEO and search costs for our new CEO.

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 and non-GAAP operating margin 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.

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Non-GAAP financial measures discussed below exclude the impact of (i) the write-down of Convio's deferred revenue balance; (ii) stock-based compensation expense; (iii) amortization of intangibles from business combinations; (iv) acquisition integration costs; (v) restructuring costs; (vi) CEO severance costs; (vii) employee severance costs; (viii) acquisition-related expenses; (ix) a write-off of proprietary software licenses; and (x) the impairment of a cost method investment, 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.

(in millions)	Year ended December 31,				
	2013	2012	Change	% Change	
GAAP revenue	\$503.8	\$447.4	\$56.4	13	%
Non-GAAP adjustments:					
Add: Convio deferred revenue write-down	1.1	5.6	(4.5)	(80)	%
Non-GAAP revenue	\$504.9	\$453.0	\$51.9	11	%
GAAP income from operations	\$51.5	\$19.4	\$32.1	165	%
GAAP operating margin	10	% 4	%		
Non-GAAP adjustments:					
Add: Convio deferred revenue writedown	1.1	5.6	(4.5)	(80)	%
Add: Stock-based compensation expense	16.9	19.2	(2.3)	(12)	%
Add: Amortization of intangibles from business combinations	24.6	17.4	7.2	41	%
Add: Acquisition integration costs	1.8	6.7	(4.9)	(73)	%
Add: Restructuring costs	3.5	0.2	3.3	1,650	%
Add: CEO severance	1.3	—	1.3	100	%
Add: Employee severance	0.6	—	0.6	100	%
Add: Acquisition-related expenses	—	6.4	(6.4)	(100)	%
Add: Write-off of prepaid proprietary software licenses	—	0.4	(0.4)	(100)	%
Add: Impairment of cost method investment	—	0.2	(0.2)	(100)	%
Total Non-GAAP adjustments	49.8	56.1	(6.3)	(11)	%
Non-GAAP income from operations	\$101.3	\$75.5	\$25.8	34	%
Non-GAAP operating margin	20	% 17	%		

The increase in non-GAAP income from operations and non-GAAP operating margin during 2013 when compared to 2012 was primarily due to (i) the inclusion of Convio's subscription-based offerings which have historically yielded higher gross margins than our historical subscription-based offerings; (ii) an increase in demand for our online fundraising offerings and our payment processing services, which have also historically yielded higher gross margins than our other offerings; and (iii) cost synergies realized from our improved operational efficiencies as we integrated the Convio operations.

Restructuring

Restructuring costs consist primarily of severance and termination benefits associated with the realignment of our workforce in response to changes in the nonprofit industry and global economy, as well as the move of our San Diego, California operations to our Austin, Texas location. We incurred \$3.2 million in before-tax restructuring charges related to the realignment of our workforce during 2013. We incurred \$0.3 million and \$0.2 million in before-tax restructuring charges related to our San Diego office transition during 2013 and 2012, respectively.

Interest expense

Interest expense remained relatively unchanged during 2013 when compared to 2012. Our interest expense is directly related to the borrowings we incurred to fund our acquisition of Convio in May 2012.

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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	December 31, 2013	December 31, 2012	Change	% Change
Maintenance	Over the term of the agreement, generally one year	\$ 85.2	\$ 81.7	\$3.5	4 %
Subscriptions	Over the term of the agreement, generally one to three years	72.5	65.9	6.6	10 %
Services	As services are delivered	32.2	36.9	(4.7)	(13)%
License fees and other	Upon delivery of the product or service	0.7	0.5	0.2	40 %
Total deferred revenue		190.6	185.0	5.6	3 %
Less: Long-term portion		9.1	11.1	(2.0)	(18)%
Current portion		\$ 181.5	\$ 173.9	\$7.6	4 %

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 and subscriptions increased during 2013 primarily as a result of an increase in renewal billings. We generally invoice our maintenance and subscription customers in annual cycles. The decrease in deferred revenue from services during 2013 was mostly due to a decrease in upfront billings on consulting arrangements. The increase in deferred revenue from license fees and other was attributable to an increase in third-party software referral fees attributable to a change in presentation from gross to net for revenue and costs associated with certain third-party software arrangements that had changes in contractual terms effective January 2013.

Comparison of the years ended December 31, 2012 and 2011

Revenue

The table below compares revenue from our consolidated statements of comprehensive income for the years ended December 31, 2012 and 2011.

(in millions)	Year ended December 31,			
	2012	2011	Change	% Change
License fees	\$20.6	\$19.5	\$1.1	6 %
Subscriptions	162.1	103.5	58.6	57 %
Services	119.6	108.8	10.8	10 %
Maintenance	136.1	130.6	5.5	4 %
Other	9.0	8.5	0.5	6 %
Total revenue	\$447.4	\$370.9	\$76.5	21 %

When removing the impact of revenue from acquired companies, revenue increased by \$21.9 million, or 6% in 2012. This increase in revenue was primarily attributable to growth in our subscriptions revenue as a result of both an increase in demand for our online fundraising offerings as well as an increase in transaction fees associated with our payment processing services. The increase in demand for our subscription offerings was primarily driven by the ongoing evolution of our product offerings from a license-based to subscription-based model. Although we continued to experience a shift in our emerging (first-time users) and mid-sized customers' buying preference away from perpetual licenses towards hosted solutions, license revenue increased in 2012 when compared to 2011 as a result of an increase in sales of our Blackbaud CRM offering to large and/or strategic customers. The increase in maintenance

revenue is attributable to maintaining high renewal rates, new maintenance contracts associated with new license agreements and increases in contracts with existing customers during 2012 when compared to 2011. Services revenue grew in 2012 principally as a result of increased demand for our education services.

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Operating results

License fees

(in millions)	Year ended December 31,				
	2012	2011	Change	% Change	
License fees revenue	\$20.6	\$19.5	\$1.1	6	%
Cost of license fees	3.0	3.3	(0.3)	(9))%
License fees gross profit	\$17.6	\$16.2	\$1.4	9	%
License fees gross margin	85	% 83	%		

Revenue from license fees increased in 2012 primarily due to a greater contribution of revenue from larger Blackbaud CRM arrangements when compared to 2011.

The decrease in cost of license fees in 2012 when compared to 2011 was principally attributable to a decrease in third-party software royalties. Third-party software royalties associated with our license-based products decreased as the demand for our perpetual license arrangements decreased and subscription-based offerings increased.

The increase in license fees gross margin during 2012 was the result of fewer sales of products that have third party software royalty costs associated with them. Additionally, the increase in revenue from Blackbaud CRM arrangements contributed to the increase in license fees gross margin during 2012.

Subscriptions

(in millions)	Year ended December 31,				
	2012	2011	Change	% Change	
Subscriptions revenue	\$162.1	\$103.5	\$58.6	57	%
Cost of subscriptions	68.8	42.5	26.3	62	%
Subscriptions gross profit	\$93.3	\$61.0	\$32.3	53	%
Subscriptions gross margin	58	% 59	%		

Included in subscriptions revenue for 2012 and 2011 was \$45.6 million and \$0.7 million of revenue attributable to acquired companies, respectively. Excluding the revenue from acquired companies, the increase in subscriptions revenue of \$13.7 million, or 13%, was principally attributable to an increase in demand for our online fundraising and data management offerings as well as an increase in transaction fees associated with our payment processing services. The increase in cost of subscriptions in 2012 was principally attributable to increases in hosting costs, human resource costs and amortization of intangibles from business combinations.

Hosting costs increased by \$8.3 million during 2012 as a result of incremental costs due to the inclusion of acquired companies. Additionally, hosting costs increased due to incremental investments to improve our hosting services and additional hosting capacity required as a result of the growth in demand for our hosted applications and other online services. Human resource costs increased \$6.6 million during 2012. The increase in human resource costs is attributable to additional headcount due to the inclusion of acquired companies and additional resources needed to support the growth in demand for our subscription-based offerings.

Amortization of intangibles from business combinations increased \$8.6 million in 2012 primarily due to the amortization expense for the acquired Convio intangible assets.

The decrease in subscriptions gross margin during 2012 compared to 2011 was primarily due to investments we made in our infrastructure, including additional headcount, expanded facilities, improved operational processes and computer equipment to support the growth in our subscription offerings.

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Services

(in millions)	Year ended December 31,				
	2012	2011	Change	% Change	
Services revenue	\$119.6	\$108.8	\$10.8	10	%
Cost of services	97.2	79.1	18.1	23	%
Services gross profit	\$22.4	\$29.7	\$(7.3)	(25)	%
Services gross margin	19	% 27	%		

Included in services revenue in 2012 and 2011 is \$9.8 million and \$0.1 million of revenue attributable to acquired companies, respectively. Excluding the revenue from acquired companies, the increase in services revenue of \$1.1 million, or 1%, is principally due to an increase in education services revenue of \$1.4 million, partially offset by a decrease in analytic services revenue of \$0.6 million. The rates we charged for our education service offerings remained relatively constant year over year and, as such, the increase in revenue was the result of a change in volume. The increase in revenue from education services was the result of higher demand for subscription-based training. Consulting services revenue remained relatively unchanged in 2012 compared to 2011 primarily due to a greater portion of our service engagements being with larger enterprise customers as our mid-market moves to subscription-based offerings. These larger enterprise engagements can experience volatility in utilization due to the complex nature of these engagements.

The increase in cost of services in 2012 is primarily attributable to an increase in human resource costs. Human resource costs increased \$12.7 million in 2012 as a result of an increase in headcount. The increase in headcount was attributable to the inclusion of additional resources from acquired companies.

An increase in allocated depreciation, facilities and IT support costs also contributed to the increase in cost of services in 2012 when compared to 2011 due to the inclusion of allocable costs from the Convio operations.

The services gross margin decreased in 2012 primarily as a result of the increases in headcount and allocated costs discussed above.

Maintenance

(in millions)	Year ended December 31,				
	2012	2011	Change	% Change	
Maintenance revenue	\$136.1	\$130.6	\$5.5	4	%
Cost of maintenance	26.0	25.2	0.8	3	%
Maintenance gross profit	\$110.1	\$105.4	\$4.7	4	%
Maintenance gross margin	81	% 81	%		

The increase in maintenance revenue in 2012 compared to 2011 was principally comprised of (i) \$12.7 million of maintenance from new customers associated with new license agreements and increases in contracts with existing customers and (ii) \$4.1 million from maintenance contract inflationary rate adjustments, partially offset by (iii) \$11.3 million from maintenance contracts that were not renewed and reductions in contracts with existing customers. Cost of maintenance increased during 2012 when compared to 2011 primarily as a result of increases in allocated costs and proprietary software costs. The increase in proprietary software costs was attributable to increases in maintenance contracts with existing customers for software products which include third-party royalty costs associated with the maintenance revenue. Maintenance gross margin in 2012 remained relatively unchanged when compared to 2011.

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Other revenue

(in millions)	Year ended December 31,			
	2012	2011	Change	% Change
Other revenue	\$9.0	\$8.5	\$0.5	6 %
Cost of other revenue	7.5	7.0	0.5	7 %
Other gross profit	\$1.5	\$1.5	\$—	— %
Other gross margin	17	% 18	%	

Other revenue increased in 2012 when compared to 2011 primarily due to an increase in fees from user conferences. Additionally, an increase in revenue from reimbursement of travel-related expenses associated with services revenue contributed to the increase in other revenue during 2012.

Cost of other revenue increased in 2012 primarily due to increases in reimbursable expenses related to services provided at customer locations. Other gross margin in 2012 remained relatively unchanged when compared to 2011.

Operating expenses

Sales and marketing

(in millions)	Year ended December 31,			
	2012	2011	Change	% Change
Sales and marketing expense	\$95.2	\$75.4	\$19.8	26 %
% of revenue	21	% 20	%	

Sales and marketing expense increased in 2012 primarily due to increases in human resource costs and commission expense. Human resource costs increased primarily due to the inclusion of additional headcount from acquired companies as well as incremental headcount to support the increase in sales and marketing efforts of our growing operations. The increase in commission expense is principally due to an increased amount of commissionable revenue in 2012.

Research and development

(in millions)	Year ended December 31,			
	2012	2011	Change	% Change
Research and development expense	\$64.7	\$47.7	\$17.0	36 %
% of revenue	14	% 13	%	

Research and development expense increased during 2012 primarily due to increased human resource and third-party contractor costs. Human resource and third-party contractor costs increased primarily due to the inclusion of additional headcount from acquired companies as well as investments we continue to make in our product development efforts, including our direct marketing offerings. Additionally, research and development costs increased during 2012 due to an increase in allocated business costs.

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General and administrative

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