BLACKBAUD INC
Form 10-Q/A
November 10, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

(Amendment No. 1)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2011

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from __________to __________.

Commission file number: 000-50600

BLACKBAUD, INC.

(Exact name of registrant as specified in its charter)

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

2000 Daniel Island Drive

Charleston, South Carolina 29492

(Address of principal executive offices, including zip code)

(843) 216-6200

(Registrant s telephone number, including area code)

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

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

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

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

The number of shares of the registrant s Common Stock outstanding as of October 26, 2011 was 44,616,308.

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Explanatory Note

The purpose of this amendment on Form 10-Q/A to Blackbaud, Inc s quarterly report on Form 10-Q for the period ended September 30, 2011, filed with the Securities and Exchange Commission on November 8, 2011, is to correct the percentage of Blackbaud s revenue for the nine months ended September 30, 2011 derived from operations outside the United States. Page 27 of the Form 10-Q inadvertently stated that percentage was approximately 20% when in fact it was approximately 14%.

This Form 10-Q/A speaks as of the original filing date of the Form 10-Q, does not reflect events that occurred subsequent to the original filing date, and does not modify or update in any way disclosures made in the original Form 10-Q.

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Item 2. Management s discussion and analysis of financial condition and results of operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q. This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements reflect our current view with respect to future events and financial performance and are subject to risks and uncertainties, including those set forth under Cautionary statement included in this Management s discussion and analysis of financial condition and results of operations and elsewhere in this report, that could cause actual results to differ materially from historical or anticipated results.

Executive summary

We provide on-premise and cloud-based 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 finances and optimize internal operations. We have focused solely on the nonprofit market since our incorporation in 1982 and have developed our suite of products and services based upon our extensive knowledge of the operating challenges facing nonprofit organizations. As of September 30, 2011, we had approximately 24,000 active customers. Our customers operate in 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 and international foreign affairs.

We derive revenue from selling perpetual licenses or charging for the use of our software products in a hosted environment and providing a broad offering of services, including consulting, training, installation and implementation, as well as ongoing customer support and maintenance. Consulting, training and implementation services 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 benchmarking studies and data modeling services.

Overall, revenue for both the third quarter of 2011 and the first nine months of 2011 increased by 15% compared to the same periods in 2010. After removing the impact of foreign currency translation and revenue from acquired companies, revenue increased by approximately 11% for both the third quarter of 2011 and the first nine months of 2011 when compared to the same periods in 2010. These increases resulted from continued growth in our subscription revenue, principally attributable to increased demand for our hosting services, online fundraising and data management offerings and the shift in our business towards hosted solutions. Also contributing to the growth in revenue is an increase in our services revenue, which is primarily due to an increase in volume of consulting and training services provided. We continue to experience declines in revenue associated with our core perpetual license offerings as a result of the continuing decreases in sales of our perpetual license offerings to the mid-market customer base, which is principally the result of customers opting to purchase our solutions under alternative packaging with more flexible subscription-based pricing. We believe this trend will continue in the future.

Income from operations for the third quarter of 2011 and the first nine months of 2011 increased by $2.6 million and $5.8 million, respectively, when compared to the same periods in 2010. The increase in income from operations is primarily attributable to growth in revenue, partially offset by (1) acquisition-related costs, (2) an increase in stock-based compensation expense and (3) an increase in sales and marketing, research and development and general and administrative expenses. The increase in these expenses is principally attributable to merit-based salary increases, an increase in commission expense associated with higher commissionable revenue and an increase in marketing costs associated with the launch of our new corporate branding and newly packaged offerings.

We ended the third quarter of 2011 with cash and cash equivalents totaling $52.0 million and no outstanding borrowings on our credit facility. During the first nine months of 2011, we generated $67.7 million in cash flow from operations, of which we used $16.5 million to acquire a business, $16.0 million to pay dividends and $13.0 million to purchase software and computer equipment.

While we have experienced growth in revenue as our market has stabilized, the global economy continues to be volatile and its impact on the nonprofit market remains uncertain. We expect that our existing and prospective customers will remain cautious in their expenditure decisions for the remainder of 2011. Notwithstanding these conditions, we remain focused on execution, investing in our key growth initiatives, strengthening our leadership position and carefully managing our costs and expenses to achieve our targeted level of profitability.

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Results of operations

Comparison of the three and nine months ended September 30, 2011 and 2010

We have included the results of operations of acquired companies in our consolidated result of operations from the date of acquisition. We have noted in the discussion below, to the extent meaningful, the impact on the comparability of our consolidated results of operations due to the inclusion of acquired companies.

We completed the acquisition of PIDI on February 1, 2011. During the first nine months of 2011, PIDI s total revenue was $5.6 million, cost of revenue was $3.5 million and operating expenses was $0.1 million.

Revenue

The table below compares revenue from our statements of operations for the three and nine months ended September 30, 2011 with the same period in 2010.

	Three months ended September 30,				Nine months ended September 30,			
(in millions)	**2011**	**2010**	**Change**	**% Change**	**2011**	**2010**	**Change**	**% Change**
License fees	$ 4.9	$ 5.1	$ (0.2)	(4)%	$ 14.6	$ 17.2	$ (2.6)	(15)%
Subscriptions	26.0	21.2	4.8	23%	77.4	60.8	16.6	27%
Services	29.8	24.0	5.8	24%	81.8	64.9	16.9	26%
Maintenance	32.9	31.4	1.5	5%	97.3	93.0	4.3	5%
Other	1.9	1.5	0.4	27%	5.1	4.2	0.9	21%
Total revenue	$ 95.5	$ 83.2	$ 12.3	15%	$ 276.2	$ 240.1	$ 36.1	15%

Total revenue increased by 15% in both the third quarter of 2011 and in the first nine months of 2011 when compared to the same periods in 2010. When removing the impact of revenue from acquired companies, revenue increased by 12% in both the third quarter of 2011 and the first nine months of 2011 when compared to the same periods in 2010. The increase in revenue is primarily attributable to growth in our subscriptions and services revenue. The increase in subscriptions revenue is primarily due to an increase in demand for our hosting services, online fundraising and data management offerings. The growth in revenue from our subscription offerings is also a result of the ongoing evolution of our product offerings from traditional perpetual license-based arrangements with upfront payments to subscription-based offerings with more flexible pricing and payments. Services revenue grew principally due to an increase in the volume of consulting services associated with implementation engagements of Blackbaud Enterprise CRM. The increase in maintenance revenue is primarily attributable to new maintenance contracts associated with new license agreements and increases in contracts with existing customers when compared to the same periods in 2010. The decrease in license fees is principally attributable to the continued shift in our customers buying preference away from traditional perpetual license-based arrangements with upfront payments to offerings with subscription-based payment arrangements.

Operating results

The operating results analyzed below are presented on a non-GAAP basis in that: the results exclude the impact of stock-based compensation expense, amortization of intangibles arising from business combinations, and gain on the sale of assets and acquisition-related expenses incurred in connection with our 2011 acquisition of PIDI. We believe that the exclusion of these costs allows us to better understand and manage our operating expenses and cash needs. These excluded costs are analyzed separately following the discussion of operating expenses.

License fees

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
License fee revenue	$ 4.9	$ 5.1	$ (0.2)	(4)%	$ 14.6	$ 17.2	$ (2.6)	(15)%
Controllable cost of license fees	0.6	0.5	0.1	20%	2.1	1.9	0.2	11%
License fee gross profit	$ 4.3	$ 4.6	$ (0.3)	(7)%	$ 12.5	$ 15.3	$ (2.8)	(18)%
License fee gross margin	88%	90%			86%	89%		

We derive revenue from license fees from the sale of our software products under a perpetual license agreement. We continue to experience a shift in our customers buying preference away from solutions offered under perpetual

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license arrangements with upfront payments to offerings with subscription-based payment arrangements. Additionally, we continue to experience long sales cycle times, delays and postponements of purchasing decisions and overall caution exercised by existing and prospective customers as a result of continued challenges posed by the economic environment. During the third quarter of 2011, revenue from license fees remained relatively unchanged when compared to the same period in 2010. During the first nine months of 2011, revenue from license fees principally decreased due to a decline in the license fee component of sales to new customers when compared to the same period in 2010.

Direct controllable cost of license fees is principally comprised of third-party software royalties and variable reseller commissions. The increase in cost of license fees in the third quarter and first nine months of 2011 compared to the same periods in 2010 is primarily attributable to higher third-party software royalties and reseller commissions. Reseller commissions have increased due to the increase in use of resellers during the first nine months of 2011 when compared to the same period in 2010.

The decrease in license fee gross margin in the third quarter of 2011 and the first nine months of 2011 when compared to the same periods in 2010 is the result of an increase in the mix of software license transactions in which we paid variable reseller commissions and had higher associated third-party software royalty costs.

Subscriptions

	Three months ended September 30,				Nine months ended September 30,			
(in millions)	**2011**	**2010**	**Change**	**% Change**	**2011**	**2010**	**Change**	**% Change**
Subscriptions revenue	$ 26.0	$ 21.2	$ 4.8	23%	$ 77.4	$ 60.8	$ 16.6	27%
Controllable cost of subscriptions	9.7	7.1	2.6	37%	27.4	20.2	7.2	36%
Subscriptions gross profit	$ 16.3	$ 14.1	$ 2.2	16%	$ 50.0	$ 40.6	$ 9.4	23%
Subscriptions gross margin	63%	67%			65%	67%		

Revenue from subscriptions is principally comprised of revenue from providing access to hosted applications and hosting services, access to certain data services and our online subscription training offerings, and variable transaction fees associated with the use of our products to fundraise online. We continue to experience growth in our hosted applications business and are increasingly experiencing a shift in our customers buying preference away from traditional perpetual licenses arrangements with upfront payment terms towards subscription based-offerings with more flexible pricing and payments. Additionally, revenue from our hosting services continues to increase as demand for these services continues to grow from both our existing and new perpetual license customers.

Excluding the impact of acquired companies, subscriptions revenue increased by $3.2 million, or 15% in the third quarter of 2011 when compared to the same period in 2010. This increase is principally attributable to the increase in demand for hosting services, online data services and data management offerings.

Subscriptions revenue for the first nine months of 2011 includes an out-of-period adjustment of $1.7 million, which increased subscriptions revenue in the first quarter of 2011, related to our accounting for subscription-based offerings that were earned in prior periods. Excluding the impact of the out-of-period adjustment and the impact of acquired companies, subscriptions revenue increased by $10.3 million, or 17% in the first nine months of 2011 when compared to the same period in 2010. This increase is principally attributable to the increase in demand for hosting services, online fundraising and data management offerings.

Controllable cost of subscriptions is primarily comprised of human resource costs, third-party royalty and data expenses, hosting expenses, an allocation of depreciation, facilities and IT support costs and other costs incurred in providing support and services to our customers. The increase in cost of subscriptions in the third quarter of 2011 and in the first nine months of 2011 compared to the same periods in 2010 is principally attributable to an increase in headcount and investments we are making in our infrastructure to support the growth in our subscription offerings. Human resource costs increased $1.6 million and $4.9 million in the third quarter of 2011 and the first nine months of 2011, respectively, compared to the same periods in 2010 as a result of the increase in headcount. Additional headcount due to the inclusion of acquired companies represented approximately $0.8 million and $2.5 million of the increase in human resource costs for the third quarter of 2011 and the first nine months of 2011, respectively. The remaining increase in headcount is due to additional resources needed to support the continued growth in this area.

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The decrease in subscriptions gross margin in the third quarter of 2011 and the first nine months of 2011 compared to the same periods in 2010 is due to an increase in the investments we are making in the infrastructure to support the growth in our subscriptions offerings.

Services

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Services revenue	$ 29.8	$ 24.0	$ 5.8	24%	$ 81.8	$ 64.9	$ 16.9	26%
Controllable cost of services	19.1	16.3	2.8	17%	56.6	46.5	10.1	22%
Services gross profit	$ 10.7	$ 7.7	$ 3.0	39%	$ 25.2	$ 18.4	$ 6.8	37%
Services gross margin	36%	32%			31%	28%		

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, selling 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. We recognize services revenue attributable to consulting services for implementation of our hosted applications and subscription offerings ratably over the related term of the hosting or subscription arrangement. We also recognize the direct and incremental costs associated with consulting services revenue ratably over the service period. However, we expense indirect costs in the period the cost is incurred.

Excluding the impact of acquired companies, services revenue increased by $4.8 million, or 20%, in the third quarter of 2011 when compared to the same period in 2010. This increase is attributable to increases in consulting services revenue of $3.3 million, education services revenue of $0.9 million and analytic services revenue of $0.6 million. The increase in consulting services revenue is principally attributable to an increase in the volume of consulting, installation and implementation services associated with our Blackbaud Enterprise CRM product offering. The rates we charge for our services offerings have remained relatively constant year over year and, as such, the increase in education and analytic services revenue is principally the result of an increase in the volume of services provided.

Included in services revenue for the first nine months of 2011 is an out-of-period adjustment recorded in the first quarter of 2011 of $0.8 million which reduced consulting services revenue. Excluding the out-of-period adjustment and the impact of acquired companies, services revenue increased by $15.5 million, or 24% in the first nine months of 2011 when compared to the same period in 2010. This increase is attributable to increases in consulting services revenue of $11.9 million, education services revenue of $2.1 million and analytic services revenue of $1.6 million. The increase in consulting services revenue is principally attributable to an increase in the volume of consulting, installation and implementation services associated with our Blackbaud Enterprise CRM product offering, which was partially offset by a reduction in the effective rates we charge as a result of a higher level of discounts offered on the sales of our consulting services during 2010. The rates we charge for our education and analytic services offerings have remained relatively constant year over year and, as such, the increase in revenue is principally the result of an increase in the volume of services provided.

Controllable cost of services is principally comprised of human resource costs, third-party contractor expenses, classroom rentals, other costs incurred in providing consulting, installation and implementation services and customer training, data expense incurred to perform analytic services and an allocation of depreciation, facilities and IT support costs. The increase in cost of services in the third quarter of 2011 and first nine months of 2011 when compared to the same periods in 2010 is primarily attributable to an increase in human resource and third-party contractor costs, which was driven by the need for additional resource capacity to meet the increasing demand for consulting services. Additionally, we continue to experience a shift in the mix of consultants to meet the needs of our enterprise customers, which require a higher level of skilled resources that carry a higher cost.

The services gross margin increased in the third quarter of 2011 and the first nine months of 2011 compared to the same periods in 2010 primarily as a result of an increase in demand for consulting services associated with our Blackbaud Enterprise CRM offering and a shift in the mix of consulting engagements to higher margin projects.

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Maintenance

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Maintenance revenue	$ 32.9	$ 31.4	$ 1.5	5%	$ 97.3	$ 93.0	$ 4.3	5%
Controllable cost of maintenance	6.1	5.8	0.3	5%	17.5	16.5	1.0	6%
Maintenance gross profit	$ 26.8	$ 25.6	$ 1.2	5%	$ 79.8	$ 76.5	$ 3.3	4%
Maintenance gross margin	81%	82%			82%	82%		

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. The increase in maintenance revenue of $1.5 million in the third quarter of 2011 compared to the same period in 2010 is principally comprised of $2.9 million of maintenance with new customers associated with new license agreements and increases in contracts with existing customers and $1.0 million from maintenance contract inflationary rate adjustments, offset by $2.4 million from maintenance contracts that were not renewed.

The increase in maintenance revenue of $4.3 million in the first nine months of 2011 compared to the same period in 2010 is principally comprised of $8.1 million of maintenance with new customers associated with new license agreements and increases in contracts with existing customers and $2.8 million from maintenance contract inflationary rate adjustments, offset by $6.6 million from maintenance contracts that were not renewed.

Controllable cost of maintenance is primarily comprised of human resource costs, third-party contractor expenses, third-party royalty costs, an allocation of depreciation, facilities and IT support costs and other costs incurred in providing support and services to our customers. The increase in cost of maintenance in the third quarter of 2011 and the first nine months of 2011 compared to the same periods in 2010 is principally attributable to an increase in human resource costs. Human resource costs increased due to merit-based salary increases, an increase in headcount and a change in the mix of support resources. Headcount increased due to an increase in volume of our new maintenance contracts and increases in our existing maintenance customer contracts. Additionally, we continue to experience a shift in the mix of support resources to meet the needs of our enterprise customers, which require a higher level of skilled resources that carry a higher cost.

The decrease in maintenance gross margin in the third quarter of 2011 compared to the same period in 2010 is due to the shift in the mix of support resources to more highly skilled resources.

Other revenue

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Other revenue	$ 1.9	$ 1.5	$ 0.4	27%	$ 5.1	$ 4.2	$ 0.9	21%
Controllable cost of other revenue	1.7	1.3	0.4	31%	4.2	3.8	0.4	11%
Other gross profit	$ 0.2	$ 0.2	$ -	0%	$ 0.9	$ 0.4	$ 0.5	125%

Other gross margin	11%	13%	18%	10%

Other revenue includes the sale of business forms that are used in conjunction with our software products, reimbursement of travel-related expenses, primarily incurred during the performance of services at customer locations, fees from user conferences and third-party software referral fees. Other revenue increased in the third quarter of 2011 and the first nine months of 2011 when compared to the same periods in 2010 primarily due to an increase in revenue from third-party software referral fees.

Controllable 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 and an allocation of depreciation, facilities and IT support costs. Other cost of revenue increased in the third quarter of 2011 and the first nine months of 2011 when compared to the same periods in 2010 primarily due to an increase in reimbursable expenses related to providing services at customer locations. The increase in other gross margin in the first nine months of 2011 is due to the increase in revenue from third-party software referral fees.

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The following schedule reconciles non-GAAP gross profit discussed above to gross profit as presented on the consolidated statements of operations:

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
License fees	$ 4.3	$ 4.6	$ (0.3)	(7)%	$ 12.5	$ 15.3	$ (2.8)	(18)%
Subscriptions	16.3	14.1	2.2	16%	50.0	40.6	9.4	23%
Services	10.7	7.7	3.0	39%	25.2	18.4	6.8	37%
Maintenance	26.8	25.6	1.2	5%	79.8	76.5	3.3	4%
Other	0.2	0.2	-	0%	0.9	0.4	0.5	125%
Total non-GAAP gross profit	$ 58.3	$ 52.2	$ 6.1	12%	$ 168.4	$ 151.2	$ 17.2	11%
Less corporate costs not allocated:								
Stock-based compensation expense	0.8	0.7	0.1	14%	2.4	2.1	0.3	14%
Amortization of intangible assets acquired in business combinations	1.6	1.5	0.1	7%	4.8	4.6	0.2	4%
Gross profit as stated in statements of operations	$ 55.9	$ 50.0	$ 5.9	12%	$ 161.2	$ 144.5	$ 16.7	12%
Gross margin %	59%	60%			58%	60%		

Operating expenses

Sales and marketing

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Sales and marketing expense excluding stock-based compensation	$ 18.4	$ 16.7	$ 1.7	10%	$ 56.2	$ 51.4	$ 4.8	9%
Add: Stock-based compensation expense	0.3	0.3	-	0%	0.9	1.0	(0.1)	(10)%
Sales and marketing expense	$ 18.7	$ 17.0	$ 1.7	10%	$ 57.1	$ 52.4	$ 4.7	9%
% of revenue (excluding stock-based compensation)	19%	20%			20%	21%		

Sales and marketing expense includes salaries and related human resource costs, travel-related expenses, sales commissions, advertising and marketing materials, public relations and an allocation of depreciation, facilities and IT support costs. Sales and marketing expense in the third quarter of 2011 compared to the same period in 2010 increased by $1.7 million primarily due to an increase in human resource costs as a result of merit-based salary increases, higher health benefit costs and an increase in headcount.

During second quarter 2010, we recorded an out-of-period adjustment of $0.8 million, which increased expense, related to our accounting for deferred sales commissions. Excluding this out-of-period adjustment, sales and marketing expense in the first nine months of 2011 compared to the same period in 2010 increased by $5.6 million, principally due to an increase of $2.1 million in commission expense and $2.8 million in human resource costs. The increase in commission expense is principally attributable to an increase in commissionable sales and revenue in

2011. Human resources costs increased primarily due to additional headcount. Additionally, marketing programs related costs increased by $0.6 million. The increase in marketing programs related costs is principally attributable to the launch of our new corporate branding and an increase in marketing costs associated with our new packaged offerings.

The decrease in sales and marketing expense as a percentage of revenue in the third quarter of 2011 when compared to the same period in 2010 is principally due to a decrease in travel and other marketing costs. The decrease in sales and marketing expense as a percentage of revenue in the first nine months of 2011 when compared to the same period in 2010 is principally due to the out-of-period adjustment recorded in 2010.

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Research and development

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Research and development expense excluding stock-based compensation	$ 11.4	$ 11.1	$ 0.3	3%	$ 33.9	$ 32.3	$ 1.6	5%
Add: Stock-based compensation	0.8	0.7	0.1	14%	2.3	2.1	0.2	10%
Research and development expense	$ 12.2	$ 11.8	$ 0.4	3%	$ 36.2	$ 34.4	$ 1.8	5%
% of revenue (excluding stock-based compensation)	12%	13%			12%	13%		

Research and development expenses include human resource costs, third-party contractor expenses, software development tools and other expenses related to developing new products, upgrading and enhancing existing products and an allocation of depreciation, facilities and IT support costs. During the third quarter of 2011 and the first nine months of 2011, the increase in research and development costs is principally attributable to an increase in human resource costs resulting from merit-based salary increases and higher health benefit costs, and the ongoing investment we are making in our products.

General and administrative

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
General and administrative expense excluding stock-based compensation, acquisition-related costs and gain on sale of assets	$ 7.3	$ 6.4	$ 0.9	14%	$ 21.6	$ 19.2	$ 2.4	13%
Add: Acquisition-related costs	-	-	-	-%	1.0	-	1.0	-%
Add: Gain on sale of assets	-	-	-	-%	(0.5)	-	(0.5)	-%
Add: Stock-based compensation	1.7	1.5	0.2	13%	5.3	4.0	1.3	33%
General and administrative expense	$ 9.0	$ 7.9	$ 1.1	14%	$ 27.4	$ 23.2	$ 4.2	18%
% of revenue (excluding stock-based compensation)	8%	8%			8%	8%		

General and administrative expense consists primarily of human resource costs for general corporate functions, including senior management, finance, accounting, legal, human resources, corporate development, third-party professional fees, insurance, an allocation of depreciation, facilities and IT support costs, and other administrative expenses. During the third quarter of 2011 and the first nine months of 2011 compared to the same periods in 2010, the increase in general and administrative expense was principally attributable to an increase in human resource costs as a result of merit-based salary increases, higher health benefit costs and an increase in bonus expense.

Stock-based compensation

We recognize compensation expense related to stock-based awards granted to employees. We measure stock-based compensation cost at the grant date based on the fair value of the award and recognize it as expense over the requisite service period, which is the vesting period.

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

Our consolidated statements of operations for the three and nine months ended September 30, 2011 and 2010 include the amounts of stock-based compensation illustrated below:

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Included in cost of revenue:								
Cost of subscriptions	$ 0.1	$ 0.1	$ -	-%	$ 0.4	$ 0.3	$ 0.1	33%
Cost of services	0.5	0.4	0.1	25%	1.4	1.2	0.2	17%
Cost of maintenance	0.2	0.2	-	-%	0.6	0.6	-	-%
Total included in cost of revenue	0.8	0.7	0.1	14%	2.4	2.1	0.3	14%
Included in operating expenses:								
Sales and marketing	0.3	0.3	-	-%	0.9	1.0	(0.1)	(10)%
Research and development	0.8	0.7	0.1	14%	2.3	2.1	0.2	10%
General and administrative	1.7	1.5	0.2	13%	5.3	4.0	1.3	33%
Total included in operating expenses	2.8	2.5	0.3	12%	8.5	7.1	1.4	20%
Total	$ 3.6	$ 3.2	$ 0.4	13%	$ 10.9	$ 9.2	$ 1.7	18%

Stock-based compensation is comprised of expense from restricted stock, performance-based restricted stock units and stock appreciation rights. The increase in stock-based compensation expense recorded in general and administrative expense during the first nine months of 2011 compared to the same period in 2010 is principally attributable to expense associated with performance-based restricted stock units, which we began granting in 2010.The table below summarizes the stock-based compensation by award type for the three and nine months ended September 30, 2011 and 2010.

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Stock-based compensation from:								
Restricted stock	$ 2.4	$ 2.2	$ 0.2	9%	$ 7.2	$ 6.5	$ 0.7	11%
Performance-based restricted stock units	0.2	-	0.2	-%	0.5	-	0.5	-%
Stock appreciation rights	1.0	1.0	-	-%	3.2	2.7	0.5	19%
Total stock-based compensation	$ 3.6	$ 3.2	$ 0.4	13%	$ 10.9	$ 9.2	$ 1.7	18%

Stock-based compensation expense increased in the third quarter of 2011 and the first nine months of 2011 compared to the same periods in 2010 due to additional grants in the fourth quarter of 2010, partially offset by the vesting of grants issued in prior years.

The total amount of compensation costs related to non-vested awards not yet recognized was $22.7 million as of September 30, 2011. This amount will be recognized as expense over a weighted average period of 1.7 years.

Amortization

We allocated amortization expense to cost of revenue based on the nature of the respective identifiable intangible asset and whether the asset is directly associated with a specific component of revenue. Amortization expense included in our consolidated statements of operations for the three and nine months ended September 30, 2011 and 2010 is illustrated below:

(in millions)	Three months ended September 30, 2011	2010	Change	% Change	Nine months ended September 30, 2011	2010	Change	% Change
Included in cost of revenue:								
Cost of license fees	$ 0.1	$ 0.1	$ -	-%	$ 0.4	$ 0.3	$ 0.1	33%
Cost of subscriptions	0.8	0.8	-	-%	2.4	2.3	0.1	4%
Cost of services	0.4	0.3	0.1	33%	1.2	1.0	0.2	20%
Cost of maintenance	0.3	0.3	-	-%	0.7	0.9	(0.2)	(22)%
Cost of other revenue	-	-	-	-%	0.1	0.1	-	-%
Total included in cost of revenue	1.6	1.5	0.1	7%	4.8	4.6	0.2	4%
Included in operating expenses	0.2	0.2	-	-%	0.7	0.6	0.1	17%
Total	$ 1.8	$ 1.7	$ 0.1	$ 6%	$ 5.5	$ 5.2	$ 0.3	$ 6%

Acquisition-related costs

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Blackbaud, Inc.

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During the first nine months of 2011, we expensed $1.0 million of acquisition-related costs, in connection with the acquisition of PIDI, which we recorded in general and administrative expense. There were no similar expenses in the first nine months of 2010.

Gain on sale of assets

During the first nine months of 2011, we recognized a gain of $0.5 million from the sale of intangible assets, which we recorded as a reduction of general and administrative expense. There was no similar transaction in the first nine months of 2010.

Income tax provision

The estimated annual effective tax rate for 2011 is 36.6%, which excludes period-specific items. Following is our effective tax rate, including the effects of period-specific items, for the three and nine months ended September 30:

	Three months ended September 30,		Nine months ended September 30,	
	2011	**2010**	**2011**	**2010**
Effective tax rate	37.3%	35.2%	34.2%	36.9%

Period-specific items recorded in the nine months ended September 30, 2011 included a decrease of $1.0 million in the valuation allowance for certain state net operating loss carryforwards, which reduced income tax expense. Period-specific items recorded in the three and nine months ended September 30, 2010 included the recognition of tax benefits related to a change in estimate for 2009 research and development credits of $0.5 million, net of reserves for uncertain tax positions.

We recorded our deferred tax assets and liabilities at an amount based upon a U.S. federal income tax rate of 35.0% and appropriate statutory tax rates of various foreign, state and local jurisdictions in which we operate. If our tax rates change in the future, we will adjust our deferred tax assets and liabilities to an amount reflecting those income tax rates. Any change will affect the provision for income taxes during the period in which the determination is made.

The amount of unrecognized tax benefit that, if recognized, would favorably affect our effective rate as of September 30, 2011 was $1.7 million. We have taken positions in certain taxing jurisdictions related to state nexus issues for which it is reasonably possible that the total amount of unrecognized tax benefits may decrease within the next twelve months. The possible decrease could result from the finalization of state income tax reviews and the expiration of statutes of limitations. The reasonably possible decrease was not material at September 30, 2011.

Liquidity and capital resources

At September 30, 2011, cash and cash equivalents totaled $52.0 million, compared to $28.0 million at December 31, 2010. The $24.0 million increase in cash and cash equivalents during the first nine months of 2011 is principally the result of cash generated from operations of $67.7 million, of which $16.5 million was used to acquire a business, $16.0 million to pay dividends and $13.0 million to purchase software and computer equipment.

Our principal source of liquidity is our operating cash flow, which depends on continued customer renewal of our maintenance, support and subscription agreements and market acceptance of our products and services. Based on current estimates of revenue and expenses, we believe that the currently available sources of funds and anticipated cash flows from operations will be adequate for at least the next twelve months to finance our operations, fund anticipated capital expenditures and pay dividends. Dividend payments are not guaranteed and our Board of Directors may decide, in its absolute discretion, at any time and for any reason, not to declare or pay further dividends and/or repurchase our common stock.

We have drawn on our credit facility from time to time to help us meet short-term financial needs, such as business acquisitions and purchase of common stock under our repurchase program. In June 2011, we entered into a new five-year $125.0 million credit facility which replaced our previous $90.0 million credit facility that was to mature in July 2012. Under the new credit facility we have three options to increase the aggregate amount available by up to $75.0 million. At September 30, 2011, we had no outstanding borrowings under our credit facility. We believe

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our cash on hand, cash generated from operations and our credit facility provides us with sufficient flexibility to meet our financial needs.

At September 30, 2011, our total cash and cash equivalents balance includes approximately $18.2 million of cash was held by operations outside the U.S. If these funds are needed for our operations in the U.S., we would be required to accrue and pay U.S. taxes to repatriate these funds. Our current plans do not demonstrate a need to repatriate them to fund our U.S. operations.

Operating cash flow

Net cash provided by operating activities of $67.7 million increased by $18.8 million during the first nine months of 2011 when compared to the same period in 2010. Throughout both periods, our cash flows from operations were derived principally from: (i) our earnings from on-going operations prior to non-cash expenses such as depreciation, amortization and stock-based compensation and adjustments to our provision for sales returns and allowances; (ii) the tax benefit associated with our deferred tax asset, which reduces our cash outlay for income tax expense; and (iii) changes in our working capital.

Working capital changes as they impact the statement of cash flows are composed of changes in accounts receivable, prepaid expenses and other assets, accounts payable, accrued expenses, accrued liabilities and deferred revenue. Cash flow from operations associated with working capital increased $7.3 million in the first nine months of 2011 when compared to the same period in 2010. This net increase is principally due to:

- an increase of $1.7 million in cash associated with accounts receivable, primarily from an increase in the collection of accounts receivable as a result the timing of billings in late 2010 as compared to late 2009; and

- a refund of income tax payments of $6.0 million.

The provision for doubtful accounts and sales returns increased $1.7 million during the nine months ended September 30, 2011 when compared to the same period in 2010. The increase is principally due to an increase in credits associated with maintenance, subscription and consulting services that is commensurate with our growth in sales. Additionally, during the first nine months of 2010, we decreased our allowance for doubtful accounts and sales returns by $0.5 million as a result of favorable returns and collections experience, which contributed to the $1.7 million year-over-year increase in cash flow from the provision for doubtful accounts and sales returns.

Investing cash flow

Net cash used in the first nine months of 2011 for investing activities was $28.6 million compared to $13.1 million in the same period in 2010. The increase is principally due to the purchase of PIDI in the first quarter of 2011. As of September 30, 2011, we spent $13.0 million on software and computer equipment associated with the infrastructure that supports our subscription-based offerings. We expect to continue making similar investments in our infrastructure and expect our full year 2011 capital expenditures to be in the range of $15.0 million to $20.0 million.

Financing cash flow

Net cash used in financing activities for the first nine months of 2011 was $14.4 million compared to $32.4 million in the same period in 2010. The decrease in cash used in financing activities is primarily due to a decrease in the purchase of treasury stock under our repurchase program. We did not repurchase any treasury shares during the nine months ended September 30, 2011, and as of September 30, 2011, $50.0 million remained available under our share repurchase program.

Commitments and contingencies

As of September 30, 2011, we had future minimum lease commitments of $61.8 million. There were no material changes outside the ordinary course of business in our contractual obligations since December 31, 2010.

We utilize third-party relationships in conjunction with our products. The contractual arrangements vary in length from one to three years. In certain cases, these arrangements require a minimum annual purchase commitment. The total remaining minimum purchase commitments under these arrangements at September 30, 2011 were $4.7 million through 2013. We incurred expense under these arrangements of $1.8 million and $1.5 million for the three months

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Blackbaud, Inc.

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

ended September 30, 2011 and 2010, respectively, and $4.4 million and $3.1 million for the nine months ended September 30, 2011 and 2010, respectively.

In February 2011, our Board of Directors approved our annual dividend rate of $0.48 per share for 2011. Dividends at the annual rate would aggregate to $21.1 million assuming 44.0 million shares of common stock are outstanding. Our ability to continue to declare and pay dividends quarterly this year and beyond might be restricted by, among other things, the terms of our credit facility, general economic conditions and our ability to generate operating cash flow.

Off-balance sheet arrangements

We do not have any off-balance sheet arrangements, financings or other relationships with unconsolidated entities or other persons.

Foreign currency exchange rates

Approximately 14% of our total net revenue for the nine months ended September 30, 2011 was derived from operations outside the United States. We do not have significant operations in countries in which the economy is considered to be highly inflationary. Our consolidated financial statements are denominated in U.S. dollars and, accordingly, changes in the exchange rate between foreign currencies and the U.S. dollar will affect the translation of our subsidiaries financial results into U.S. dollars for purposes of reporting our consolidated financial results. The accumulated currency translation adjustment, recorded as a separate component of stockholders equity, was $0.7 million and $0.5 million at September 30, 2011 and December 31, 2010, respectively.

The vast majority of our contracts are entered into by our U.S., Canadian or U.K. entities. The contracts entered into by the U.S. entity are almost always denominated in U.S. dollars, contracts entered into by our Canadian subsidiary are generally denominated in Canadian dollars, and contracts entered into by our U.K., Australian and Netherlands subsidiaries are generally denominated in pounds sterling, Australian dollars and Euros, respectively. Historically, as the U.S. dollar weakened, foreign currency translation resulted in an increase in our revenues and expenses denominated in non-U.S. currencies. During third quarter 2011, foreign translation resulted in an increase in our revenues and expenses denominated in non-U.S. currencies. Though we do not believe our exposure to currency exchange rates have had a material impact on our consolidated results of operations or financial position, we intend to continue to monitor such exposure and take action as appropriate.

Cautionary statement

We operate in a highly competitive environment that involves a number of risks, some of which are beyond our control. The following statement highlights some of these risks.

Statements contained in this Form 10-Q, which are not historical facts, are or might constitute forward-looking statements under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Although we believe the expectations reflected in such forward-looking statements are based on reasonable assumptions, we can give no assurance that our expectations will be attained. Forward-looking statements involve known and unknown risks that could cause actual results to differ materially from expected results. Factors that could cause actual results to differ materially from our expectations expressed in the report include: general economic risks; lengthy sales and implementation cycles, particularly in larger organizations; uncertainty regarding increased business and renewals from existing customers; continued success in sales growth; management of integration of recently acquired companies and other risks associated with acquisitions; the ability to attract and retain key personnel, including our new CFO; risk associated with successful implementation of multiple integrated software products; risks related to our dividend policy and stock repurchase program, including potential limitations on our ability to grow and the possibility that we might discontinue payment of dividends; risks relating to restrictions imposed by the credit facility; risks associated with management of growth; technological changes that make our products and services less competitive; and the other risk factors set forth from time to time in our SEC filings.

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Item 6. Exhibits

Exhibits:

31.1	Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by the Chief Executive Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by the Chief Financial Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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Blackbaud, Inc.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

	BLACKBAUD, INC.
Date: November 10, 2011	By: /s/ Marc E. Chardon Marc E. Chardon President and Chief Executive Officer
Date: November 10, 2011	By: /s/ Timothy V. Williams Timothy V. Williams Senior Vice President and Chief Financial Officer