Bridgeline Digital, Inc.
Form 10-Q
May 15, 2013

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

Form 10-Q

(Mark One)
x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2013

OR

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______________ to ______________

Commission File Number 333-139298

Bridgeline Digital, Inc.
(Exact name of registrant as specified in its charter)

Delaware State or other jurisdiction of incorporation or organization	52-2263942 IRS Employer Identification No.
80 Blanchard Road Burlington, Massachusetts (Address of Principal Executive Offices)	01803 (Zip Code)

(781) 376-5555
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files) x Yes o 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 definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

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

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

The number of shares of Common Stock par value $0.001 per share, outstanding as of May 10, 2013 was 15,332,968

1

Bridgeline Digital, Inc.

Quarterly Report on Form 10-Q

For the Quarterly Period ended March 31, 2013

Index

Bridgeline Digital, Inc.

Quarterly Report on Form 10-Q

For the Quarterly Period ended March 31, 2013

Statements contained in this Report on Form 10-Q that are not based on historical facts are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may be identified by the use of forward-looking terminology such as “should,” “could,” “may,” “will,” “expect,” “beli “estimate,” “anticipate,” “intends,” “continue,” or similar terms or variations of those terms or the negative of those terms. These statements appear in a number of places in this Form 10-Q and include statements regarding the intent, belief or current expectations of Bridgeline Digital, Inc. Forward-looking statements are merely our current predictions of future events. Investors are cautioned that any such forward-looking statements are inherently uncertain, are not guaranties of future performance and involve risks and uncertainties. Actual results may differ materially from our predictions. Important factors that could cause actual results to differ from our predictions include the impact of the weakness in the U.S. and international economies on our business, our inability to manage our future growth effectively or profitably, fluctuations in our revenue and quarterly results, our license renewal rate, the impact of competition and our ability to maintain margins or market share, the limited market for our common stock, the volatility of the market price of our common stock, the performance of our products, our ability to respond to rapidly evolving technology and customer requirements, our ability to protect our proprietary technology, the security of our software, our dependence on our management team and key personnel, our ability to hire and retain future key personnel, or our ability to maintain an effective system of internal controls. Although we have sought to identify the most significant risks to our business, we cannot predict whether, or to what extent, any of such risks may be realized, nor is there any assurance that we have identified all possible issues which we might face. We assume no obligation to update our forward-looking statements to reflect new information or developments. We urge readers to review carefully the risk factors described in our Annual Report on Form 10-K for the fiscal year ended September 30, 2012 as well as in the other documents that we file with the Securities and Exchange Commission. You can read these documents at www.sec.gov.

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

PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.

BRIDGELINE DIGITAL, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except share and per share data)
(Unaudited)

	March 31, 2013	September 30, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$1,799	$2,126
Accounts receivable and unbilled receivables, net	3,742	3,977
Prepaid expenses and other current assets	821	648
Total current assets	6,362	6,751
Equipment and improvements, net	2,541	2,735
Intangible assets, net	1,142	1,527
Goodwill	21,880	21,545
Other assets	1,742	1,132
Total assets	$33,667	$33,690
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$1,159	$1,132
Accrued liabilities	1,062	1,306
Accrued earnouts, current	399	375
Debt, current	1,342	1,424
Capital lease obligations, current	227	230
Deferred revenue	2,996	1,144
Total current liabilities	7,185	5,611
Accrued earnouts, net of current portion	616	990
Debt, net of current portion	2,890	2,988
Capital lease obligations, net of current portion	112	127
Other long term liabilities	952	1,004
Total liabilities	$11,755	$10,720
Commitments and contingencies		
Stockholders' equity:		
Preferred stock - $0.001 par value; 1,000,000 shares authorized; none issued and outstanding	-	-
Common stock -$0.001 par value; 20,000,000 shares authorized; 15,332,968 and 15,203,538 shares issued and outstanding, respectively	15	15
Additional paid-in capital	41,067	40,847

Accumulated deficit	(19,045)	(17,716)
Accumulated other comprehensive loss	(125)	(176)
Total stockholders’ equity	21,912	22,970
Total liabilities and stockholders’ equity	$33,667	$33,690

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

BRIDGELINE DIGITAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in thousands, except share and per share data)
(Unaudited)

	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Six Months Ended March 31, 2013	Six Months Ended March 31, 2012
Revenue:				
Web application development services	$4,489	$5,441	$9,339	$10,749
Managed service hosting	491	611	1,047	1,227
Subscription and perpetual licenses	1,024	620	1,811	1,213
Total revenue	6,004	6,672	12,197	13,189
Cost of revenue:				
Web application development services	2,494	2,771	5,248	5,626
Managed service hosting	76	85	148	191
Subscription and perpetual licenses	247	100	415	220
Total cost of revenue	2,817	2,956	5,811	6,037
Gross profit	3,187	3,716	6,386	7,152
Operating expenses:				
Sales and marketing	2,164	1,846	3,998	3,561
General and administrative	946	1,001	2,300	2,001
Research and development	247	480	379	883
Depreciation and amortization	390	435	814	850
Impairment of intangible asset	-	-	-	281
Total operating expenses	3,747	3,762	7,491	7,576
Loss from operations	(560)	(46)	(1,105)	(424)
Interest income (expense), net	(59)	(72)	(135)	(136)
Loss before income taxes	(619)	(118)	(1,240)	(560)
Provision for income taxes	68	48	89	69
Net loss	$(687)	$(166)	$(1,329)	$(629)
Net loss per share:				
Basic and diluted	$(0.05)	$(0.01)	$(0.09)	$(0.05)
Number of weighted average shares:				
Basic and diluted	14,878,361	12,338,156	14,830,488	12,328,899

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

BRIDGELINE DIGITAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in thousands, except share and per share data)
(Unaudited)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	2012	2013	2012
Net Loss	$(687)	$(166)	$(1,329)	$(629)
Other comprehensive income (loss):				
Net change in foreign currency translation adjustment	12	(30)	51	(36)
Other comprehensive income (loss):	12	(30)	51	(36)
Comprehensive loss	$(675)	$(196)	$(1,278)	$(665)

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

BRIDGELINE DIGITAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

	Six Months Ended March 31, 2013	Six Months Ended March 31, 2012
Cash flows from operating activities:		
Net loss	$(1,329)	$(629)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Amortization of intangible assets	274	386
Impairment of intangible asset	-	281
Depreciation	540	464
Other amortization	79	90
Stock-based compensation	279	155
Contingent earnout liability adjustment	(312)	(313)
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable and unbilled receivables	199	833
Prepaid expenses and other assets	(116)	(209)
Accounts payable and accrued liabilities	(410)	(745)
Deferred revenue	1,828	(134)
Other liabilities	(52)	(139)
Total adjustments	2,309	669
Net cash provided by operating activities	980	40
Cash flows from investing activities:		
Equipment and improvements	(239)	(580)
Acquisitions, net of cash acquired	-	(33)
Software development capitalization costs	(670)	(14)
Contingent acquisition payments	(237)	(261)
Net cash used in investing activities	(1,146)	(888)
Cash flows from financing activities:		
Proceeds from exercise of employee stock options	67	20
Proceeds from employee stock purchase plan	46	-
Borrowings from bank term loan	-	-
Borrowings from bank line of credit	725	1,875
Payments on bank term loan	(183)	(172)
Payments on bank line of credit	(610)	(1,677)
Payments on acquired debt	-	(120)
Payments on subordinated promissory notes	(112)	(83)
Principal payments on capital leases	(145)	(135)
Net cash used in financing activities	(212)	(292)
Effect of exchange rate changes on cash and cash equivalents	51	(36)
Net decrease in cash and cash equivalents	(327)	(1,176)
Cash and cash equivalents at beginning of period	2,126	2,528
Cash and cash equivalents at end of period	$1,799	$1,352
Supplemental disclosures of cash flow information:		
Cash paid for:		
Interest	$135	$130

Income taxes	$13	$34
Non cash activities:		
Equipment purchased under capital leases	$123	$104
Equipment and other assets included in accounts payable	$-	$237
Accrued contingent consideration (earnouts)	$83	$600
Common stock issued in connection with acquisition	$-	$150

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

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

1. Description of Business

Overview

Bridgeline Digital enables its customers to maximize the performance of their mission critical websites, intranets, and online stores. Bridgeline is the developer of the award-winning iAPPS Web Engagement Management (WEM) product platform and related digital solutions. The iAPPS platform deeply integrates Web Content Management, eCommerce, eMarketing, and web Analytics capabilities within the heart of websites or eCommerce web stores to help marketers deliver online experiences that attract, engage, and convert their customers across all digital channels. Bridgeline's iAPPS platform combined with its digital services assists customers in maximizing on-line revenue, improving customer service and loyalty, enhancing employee knowledge, and reducing operational costs.

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

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

Locations

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

2. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

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

Unaudited Interim Financial Information

The accompanying interim Condensed Consolidated Balance Sheet as of March 31, 2013, the Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2013 and 2012, respectively, the Condensed and Consolidated Statements of Comrpehensive Income for the three and six months ended March 31, 2013 and 2012, respectively, and the Condensed Consolidated Statements of Cash Flows for the six months ended March 31, 2013 and 2012, respectively, are unaudited. The unaudited interim condensed consolidated statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP") and in the opinion of the Company's management have been prepared on the same basis as the audited consolidated financial statements as of and for the year ended September 30, 2012. These condensed financial statements include all adjustments, consisting of normal recurring adjustments and accruals, necessary for the fair presentation of the Company's financial position at March 31, 2013 and its results of operations for the three and six months ended March 31, 2013 and 2012, respectively, and its cash flows for the six months ended March 31, 2013 and 2012, respectively. The results for the three months ended March 31, 2013 are not necessarily indicative of the results to be expected for the year ending September 30, 2013. The accompanying September 30, 2012 Condensed Consolidated Balance Sheet has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by US GAAP for complete financial statements.

Subsequent Events

On May 3, 2013 the Company amended its charter to increase the number of authorized common shares from 20 million to 30 million.

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update No. 2011-05 (“ASU 2011-05”), Presentation of Comprehensive Income, which amends ASC Topic 220, Comprehensive Income. ASU 2011-05 eliminates the option to present the components of other comprehensive income as a part of the statement of stockholders’ equity and requires other comprehensive income to be presented as part of a single continuous statement of comprehensive income or in a statement of other comprehensive income immediately following the statement of operations. While the new guidance changes the presentation of comprehensive income, there are no changes to the components that are recognized in net income or other comprehensive income. ASU 2011-05 is effective for fiscal years beginning after December 15, 2011 and must be retrospectively applied to all reporting periods presented. The Company adopted ASU 2011-05 on October 1, 2012. The adoption of ASU 2011-05 did not have an impact on the Company’s financial condition, results of operations or cash flows.

3. Accounts Receivable and Unbilled Receivables

Accounts receivable and unbilled receivables consists of the following:

	As of March 31, 2013	As of September 30, 2012
Accounts receivable	$ 3,451	$ 3,794
Unbilled receivables	384	381
Subtotal	3,835	4,175
Allowance for doubtful accounts	(93)	(198)
Accounts receivable and unbilled receivables, net	$ 3,742	$ 3,977

4. Acquisitions

MarketNet, Inc.

On May 31, 2012, the Company completed the acquisition of MarketNet, Inc. (“MarketNet”), an interactive technology company that provides web application development based in Dallas, Texas. The Company acquired all of the outstanding capital stock of MarketNet for consideration consisting of (i) $20 thousand in cash, (ii) assumption of debt of $244 thousand and (ii) contingent consideration of up to $650 thousand in cash and 204,331 shares of Bridgeline Digital common stock, valued at $250 thousand ($1.22 per share). The cash consideration was reduced by $58 thousand due to the Seller’s inability to meet an agreed upon target for working capital at the time of acquisition and was applied against Marketnet’s earnout payment for the three months ended December 31, 2012. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain quarterly revenue and quarterly operating income targets during the period. To the extent that either the quarterly revenue target or the quarterly operating income target is not met in a particular quarter, the earn-out period will be extended for up to four additional quarters. MarketNet is also eligible to earn additional bonus equity consideration of 200,000 shares, if annual net revenues of the acquired business exceed a certain threshold in any fiscal year through September 30, 2015. The Company is required to assess the probability of the acquired business achieving the contingent cash and stock payments which requires management to make estimates and judgments based on forecasts of future performance. As a result, the Company reduced the initial estimate of $607 thousand for the contingent cash consideration to be achieved and $262 thousand for the contingent stock consideration to be achieved by $8 thousand and $30 thousand, respectively. The contingent common stock has been issued and is being held in escrow pending satisfaction of the applicable targets. MarketNet achieved its quarterly revenue and operating income targets for the first two quarterly periods after the acquisition date but not for the three months ended March 31, 2013. MarketNet's operating results are reflected in the Company's condensed consolidated financial statements as of the acquisition date.

Magnetic Corporation

On October 3, 2011, the Company completed the acquisition of Magnetic Corporation ("Magnetic"), a web technology company based in Tampa, Florida. Bridgeline acquired all of the outstanding capital stock of Magnetic for consideration consisting of (i) $150 thousand in cash and (ii) contingent consideration of up to $600 thousand in cash and 166,666 shares of Bridgeline Digital common stock, valued at $150 thousand ($0.90 per share). The cash consideration was reduced by $100 thousand due to the Seller's inability to meet an agreed upon target for working capital at the time of acquisition. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain quarterly revenue and quarterly operating income targets during the period. The contingent common stock has been issued and is being held in escrow pending satisfaction of the applicable targets. To the extent that either the quarterly revenue target or the quarterly operating income target is not met in a particular quarter, the earn-out period will be extended for up to four additional quarters. The Company is required to assess the probability of the acquired business achieving the contingent cash and stock payments which requires management to make estimates and judgments based on forecasts of future performance. As a result, the Company estimated and accrued $600 thousand of the contingent cash consideration to be achieved and $150 thousand of the contingent stock consideration to be achieved. Magnetic achieved its quarterly revenue and operating income targets for all periods since the acquisition date. Magnetic's operating results are reflected in the Company's condensed consolidated financial statements as of the acquisition date, which corresponds to the Company's commencement of fiscal 2012.

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

The estimated fair value of net assets acquired from the MarketNet and Magnetic acquisitions are summarized as follows:

Net assets acquired:		Amount
Cash	$	35
Accounts Receivable, net		327
Other Assets		181
Fixed Assets		91
Intangible Assets		910
Goodwill		1,426
Total Assets		2,970
Current Liabilities		1,210
Liabilities, net of current		73
Total liabilities assumed		1,283
Net assets acquired:	$	1,687
Purchase Price:		
Cash Paid	$	70
Contingent earnouts - payable in cash		1,206
Contingent earnouts - payable in common stock		411
	$	1,687

As part of the Magnetic acquisition, of the $430 thousand allocated to intangible assets, $350 thousand is allocated to customer relationships and $80 thousand is allocated to non-compete agreements, with an average useful life of five years.

The Company completed its formal valuation of intangibles acquired in the MarketNet transaction during the three months ended March 31, 2013. As a result, the Company's initial estimate of $600 thousand allocated to intangible assets was reduced to $480 thousand. $370 thousand was allocated to customer relationships with and estimated useful life of 5 years and $110 thousand allocated to non-compete agreements with an estimated useful life of 7 years.

The goodwill recorded as a result of the Magnetic and MarketNet acquisitions is nondeductible for tax purposes.

The following unaudited pro forma financial information reflects the combined results of operations for Bridgeline for the three and six months ended March 31, 2012, including certain adjustments, as if the acquisition of MarketNet had occurred on October 1, 2011. This information does not necessarily reflect the results of operations that would have occurred had the acquisitions taken place at the beginning of the period, and is not necessarily indicative of the results which may be obtained in the future (in thousands, except per share data):

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

	Three Months Ended March 31, 2013	Six Months Ended March 31, 2013
Total revenue	$ 7,285	$ 14,455
Net loss	$ (149)	$ (681)
Net loss per share:		
Basic and diluted	$ (0.01)	$ (0.06)
Number of weighted average shares:		
Basic and diluted	12,355,184	12,345,928

Contingent earnout liabilities for acquisitions completed after September 30, 2009 were recorded at fair value based on valuation models that utilize relevant factors such as estimated probabilities of the acquisitions achieving the performance targets throughout the earnout period. During the three months ended March 31, 2013, total estimated contingent earnout liabilities, cash and stock, were reduced by $312 thousand which comprised $141 thousand of contingent cash earnouts and $171 thousand of contingent stock earnouts. The following table summarizes the changes in accrued earnout liabilities for the six months ended March 31, 2013:

Balance at September 30, 2012	$ 1,365
Contingent earnout liability accruals	83
Contingent earnout liability payments	(237)
Contingent earnout reduced by working capital adjustment	(55)
Contingent earnout liability estimate adjustment	(141)
Balance at March 31, 2013	$ 1,015

5. Intangible Assets

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

	As of March 31, 2013			
	Gross Amount	Accumulated Amortization	Impairment	Net Amount
Intangible assets:				
Domain and trade names	$ 26	$ (26)	$ -	$ -
Customer related	4,126	(2,876)	(281)	969
Non-compete agreements	827	(654)	-	173
Acquired software	362	(362)	-	-
Total intangible assets	$ 5,341	$ (3,918)	$ (281)	$ 1,142

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

	As of September 30, 2012			
	Gross Amount	Accumulated Amortization	Impairment	Net Amount
Intangible assets:				
Domain and trade names	$ 26	$ (26)	$ -	$ -
Customer related	4,187	(2,654)	(281)	1,252
Non-compete agreements	877	(602)	-	275
Acquired software	362	(362)	-	-
Total intangible assets	$ 5,452	$ (3,644)	$ (281)	$ 1,527

Total amortization expense related to intangible assets for the three months ended March 31, 2013 and 2012 was $118 thousand and $191 thousand, respectively, and amortization expense related to intangible assets for the six months ended March 31, 2013 and 2012 was $274 thousand and $386 thousand, respectively. They are reflected in operating expenses on the Condensed Consolidated Statements of Operations.

6. Goodwill

Changes in the carrying amount of goodwill follows:

	As of March 31, 2013	As of September 30, 2012
Balance at beginning of period	$ 21,545	$ 20,122
Acquisitions	-	1,175
Contingent acquisition payments	83	248
Purchase price allocation adjustments	252	-
Balance at end of period	$ 21,880	$ 21,545

7. Debt

Bank Term Loan

In March 2010, the Company entered into an Amended and Restated Loan and Security Agreement SVB (the “Loan Agreement”) with Silicon Valley Bank (“SVB”). The Loan Agreement has a two year term which expired on March 31, 2012. In May 2011, the Company amended its loan arrangement (the “Amendment”) with SVB, extending the maturity date of the line of credit for one year to March 31, 2013. The Amendment also revised certain financial covenants and amended the out of formula borrowings to be structured as a $2 million term loan and interest on the term loan will be at SVB’s prime rate plus 1.75%. In May 2012, the Company amended its loan agreement (the “2012 Amendment”) with SVB, extending the maturity date of the line of credit for one year to March 31, 2014. The 2012 Amendment also revised certain financial covenants. In February 2013, the Company amended its loan agreement (the “2013 Amendment”) with SVB, extending the maturity date of the line of credit for one year to March 31, 2015. The 2013 Amendment also revised certain financial covenants. The Company would not have been in compliance with one of its covenants for the three months ended December 31, 2012 if the amendment was not completed. The Company was compliant with its financial covenants as of March 31, 2013.

Promissory Notes

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

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

Debt consists of the following:

	As of March 31, 2013	As of September 30, 2012
Line of credit borrowings	$ 2,496	$ 2,382
Bank term loan	1,510	1,692
Subordinated promissory notes	226	338
Total debt	$ 4,232	$ 4,412
Less current portion	$ 1,342	$ 1,424
Long term debt, net of current portion	$ 2,890	$ 2,988

8. Other Long Term Liabilities

Deferred Rent

In connection with new leases for the Company's headquarters in Burlington, Massachusetts and a new location in New York, the Company made investments in leasehold improvements at these locations of approximately $1.4 million, of which the respective landlords funded approximately $857 thousand. The capitalized leasehold improvements are being amortized over the initial lives of each lease. The improvements funded by the landlords are treated as lease incentives. Accordingly, the funding received from the landlords was recorded as fixed asset additions and a deferred rent liability on the Condensed Consolidated Balance Sheet. As of March 31, 2013, $121 thousand was reflected in Accrued Liabilities and $580 thousand is reflected in Other Long Term Liabilities. The deferred rent liability is being amortized as a reduction of rent expense over the lives of the leases.

9. Shareholder's Equity

Common Stock

On May 31, 2012, the Company sold 2,173,913 shares of common stock at $1.15 per share for gross proceeds of $2.5 million in a private placement. Net proceeds to the Company after offering expenses were approximately $2.3 million. In addition, the Company issued the placement agent and its affiliates five year warrants to purchase an aggregate of 217,913 shares of Bridgeline's common stock at a price equal to $1.40 per share. The Company agreed to provide piggyback registration rights with respect to the shares of common stock sold in the offering and underlying the warrants.

In connection with the acquisition of MarketNet on May 31, 2012, contingent consideration of 204,331 shares of Bridgeline Digital common stock is contingently issuable to the sole stockholder of MarketNet. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain operating and revenue targets. The common stock has been issued and is being held in escrow pending satisfaction of the applicable earnout targets. In addition, MarketNet is also eligible to earn additional bonus equity consideration of 200,000 shares of Bridgeline Digital common stock if a certain annual revenue threshold is met in any fiscal year during the next three years. As of March 31, 2013, the sole stockholder of

MarketNet had earned 34,056 shares of common stock.

In connection with the acquisition of Magnetic Corporation on October 3, 2011, contingent consideration of 166,666 shares of Bridgeline Digital common stock is contingently issuable to the sole stockholder of Magnetic. The contingent consideration is payable quarterly over the 12 consecutive calendar quarters following the acquisition, contingent upon the acquired business achieving certain operating and revenue targets. The common stock has been issued and is being held in escrow pending satisfaction of the applicable earnout targets. As of March 31, 2013, the sole stockholder of Magnetic had earned 83,334 shares of common stock.

BRIDGELINE DIGITAL, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share and per share data)

Employee Stock Purchase Plan

On April 12, 2012, the Company's stockholders approved and adopted the Bridgeline Digital, Inc. 2012 Employee Stock Purchase Plan (the "ESPP"). Under the terms of the ESPP, the Company will grant eligible employees the right to purchase shares of Bridgeline common stock through payroll deductions at a price equal to 85% of the fair market value of Bridgeline common stock on the purchase termination date of defined offering or purchase periods. Each offering period is six months in duration. The ESPP permits the Company to offer up to 300,000 shares of common stock. The maximum number of shares of common stock that may be purchased by all participants in any purchase period may not exceed 150,000 shares. During the six months ended March 31, 2013, 24,964 shares were purchased by employees.

Common Stock Warrants

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

On October 29, 2010, the Company issued four year warrants to the placement agent in the Company's private placement. The warrants are exercisable to purchase 64,000 shares of the Company's common stock at a price equal to $1.45 per share. In return for such warrants, the placement agent agreed to cancel 71,231 warrants issued to the placement agent in April 2006 and 57,000 IPO Warrants. In December 2012 all 64,000 warrants were exercised using a cashless feature where the holders forfeited 41,401 shares in lieu of paying the exercise price.

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

Summary of Option and Warrant Activity and Outstanding Shares

	Stock Options		Stock Warrants	
	Options	Weighted Average Exercise Price	Warrants	Weighted Average Exercise Price
Outstanding, September 30, 2012	2,989,620	$0.86	331,931	$1.42
Granted	391,500	$1.70	-	-
Exercised	(75,367)	$0.90	(22,599)	$1.45
Forfeited or expired	(88,002)	$1.23	(41,401)	$1.45
Outstanding, March 31, 2013				