Bridgeline Digital, Inc.
Form 10-Q
February 14, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2018

OR

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

For the transition period from ______________ to ______________

Commission File Number 333-139298

Bridgeline Digital, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**52-2263942**
State or other jurisdiction of incorporation or organization	IRS Employer Identification No.

100 Summit Drive	
Burlington, Massachusetts	**01803**
(Address of Principal Executive Offices)	(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 No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files) Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	
	Smaller reporting company
	Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares of Common Stock par value $0.001 per share, outstanding as of February 10, 2019 was 14,181,259.

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Bridgeline Digital, Inc.

Quarterly Report on Form 10-Q

For the Quarterly Period ended December 31, 2018

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Bridgeline Digital, Inc.

Quarterly Report on Form 10-Q

For the Quarterly Period ended December 31, 2018

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," "believe," "estimate," "anticipate," "intends," "continue," or similar terms or variations of those terms or the negative of those terms. These statements appear in a number of places in this Form 10-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 ability to maintain our listing on the NASDAQ Capital market, the ability to raise capital, the performance of our products, our ability to respond to rapidly evolving technology and customer requirements, our ability to protect our proprietary technology, dependence on third parties, the security of our software and response to cyber security risks, our ability to meet our financial obligations and commitments, 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, and our ability to respond to government regulations. 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, 2018 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. Condensed Consolidated Financial Statements.

BRIDGELINE DIGITAL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

(Unaudited)

	December 31, 2018	September 30, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ *2,101*	$ *644*
Accounts receivable and unbilled receivables, net	*2,267*	*1,721*
Prepaid expenses	*472*	*452*
Other current assets	*75*	*21*
Total current assets	*4,915*	*2,838*
Property and equipment, net	*57*	*80*
Intangible assets, net	*17*	*20*
Goodwill	*4,050*	*7,782*
Other assets	*232*	*280*
Total assets	$ *9,271*	$ *11,000*
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ *1,215*	$ *1,577*
Accrued liabilities	*480*	*580*
Debt, current	*198*	*1,017*
Deferred revenue	*935*	*594*
Total current liabilities	*2,828*	*3,768*
Debt, net of current portion	*2,323*	*2,574*
Other long term liabilities	*203*	*234*
Total liabilities	*5,354*	*6,576*
Commitments and contingencies		

Stockholders' equity:		
Preferred stock - $0.001 par value; 1,000,000 shares authorized;		
Series A Convertible Preferred stock:		
264,000 shares and 262,310 shares at December 31, 2018 and 264,000 shares and 262,364 shares at September 30, 2018 issued and outstanding (liquidation preference $2,624 at December 31, 2018)	-	-
Series B Convertible Preferred stock:		
4,288 shares and 80 shares at December 31, 2018 and 0 shares at September 30, 2018 issued and outstanding	-	-
Common stock - $0.001 par value; 50,000,000 shares authorized; 14,081,259 shares and 4,241,225 shares at December 31, 2018 and at September 30, 2018 issued and outstanding	*14*	*5*
Additional paid-in capital	*70,988*	*66,548*
Accumulated deficit	*(66,734*)	*(61,778*)
Accumulated other comprehensive loss	*(351*)	*(351*)
Total stockholders' equity	*3,917*	*4,424*
Total liabilities and stockholders' equity	$ *9,271*	$ *11,000*

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

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BRIDGELINE DIGITAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except share and per share data)

(Unaudited)

	Three Months Ended December 31,	
	2018	**2017**
Net revenue:		
Digital engagement services	$ *1,073*	$ *2,060*
Subscription and perpetual licenses	*1,045*	*1,606*
Managed service hosting	*257*	*303*
Total net revenue	*2,375*	*3,969*
Cost of revenue:		
Digital engagement services	*855*	*1,397*
Subscription and perpetual licenses	*423*	*480*
Managed service hosting	*63*	*80*
Total cost of revenue	*1,341*	*1,957*
Gross profit	*1,034*	*2,012*
Operating expenses:		
Sales and marketing	*814*	*1,030*
Support	*91*	*74*
General and administrative	*687*	*736*
Research and development	*418*	*407*
Depreciation and amortization	*26*	*108*
Goodwill impairment	*3,732*	-
Total operating expenses	*5,768*	*2,355*
Loss from operations	*(4,734*)	*(343*)
Interest and other expense, net	*(217*)	*(86*)
Loss before income taxes	*(4,951*)	*(429*)
Provision for income taxes	*4*	*1*
Net loss	*(4,955*)	*(430*)
Dividends on convertible preferred stock	*(79*)	*(75*)
Net loss applicable to common shareholders	$ *(5,034*)	$ *(505*)
Net loss per share attributable to common shareholders:		
Basic and diluted	$ *(0.46*)	$ *(0.12*)
Number of weighted average shares outstanding:		
Basic and diluted	*11,007,780*	*4,200,219*

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

BRIDGELINE DIGITAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(in thousands)

(Unaudited)

	Three Months Ended December 31,	
	2018	**2017**
Net Loss	$*(4,955*)	$*(430*)
Other Comprehensive Income : Net change in foreign currency translation adjustment	-	*1*
Comprehensive loss	$*(4,955*)	$*(429*)

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

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BRIDGELINE DIGITAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Three Months Ended December 31,	
	2018	**2017**
Cash flows from operating activities:		
Net loss	$*(4,955)*	$*(430)*
Adjustments to reconcile net loss to net cash used in operating activities:		
Loss on disposal of property and equipment	*9*	-
Amortization of intangible assets	*4*	*72*
Depreciation	*20*	*36*
Other amortization	*15*	*16*
Goodwill impairment	*3,732*	-
Debt discount amortization	*150*	*22*
Change in fair value of warrant	*(12)*	-
Stock-based compensation	*97*	*125*
Changes in operating assets and liabilities		
Accounts receivable and unbilled receivables	*(546)*	*(182)*
Prepaid expenses	*28*	*(55)*
Other current assets and other assets	*(10)*	*5*
Accounts payable and accrued liabilities	*(499)*	*(37)*
Deferred revenue	*344*	*(86)*
Other liabilities	*68*	*(61)*
Total adjustments	*3,400*	*(145)*
Net cash used in operating activities	*(1,555)*	*(575)*
Cash flows from investing activities:		
Software development capitalization costs	*(11)*	-
Purchase of property and equipment	*(7)*	*(8)*
Net cash used in investing activities	*(18)*	*(8)*
Cash flows from financing activities:		
Proceeds from issuance of common stock and Series B convertible preferred stock, net of issuance costs	*4,376*	-
Proceeds from term notes from Montage Capital, net of issuance costs	-	*953*
Borrowing on bank line of credit	-	*300*
Payments on bank line of credit	*(201)*	*(300)*
Principal payments on term notes from Montage Capital	*(125)*	-

Principal payments on promissory term notes	(941)	-
Cash dividends paid on Series A convertible preferred stock	(79)	-
Net cash provided by financing activities	3,030	953
Effect of exchange rate changes on cash and cash equivalents	-	(1)
Net increase in cash and cash equivalents	1,457	369
Cash and cash equivalents at beginning of period	644	748
Cash and cash equivalents at end of period	$2,101	$1,117
Supplemental disclosures of cash flow information:		
Cash paid for:		
Interest	$185	$64
Income taxes	$4	$9
Non cash investing and financing activities:		
Accrued dividends on convertible preferred stock	$-	$76

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

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

1. **Description of Business**

Overview

Bridgeline Digital, The Digital Engagement Company™ (the “Company”), helps customers with their digital experience from websites and intranets to eCommerce experiences. The Bridgeline Unbound platform is delivered through a cloud-based SaaS (“Software as a Service”) multi-tenant business model, providing maintenance, daily technical operation and support; or via a traditional perpetual licensing business model, in which the software resides on a dedicated server in either the customer’s facility or hosted by Bridgeline via a cloud-based hosted services model.

The Company 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 has *one* wholly-owned subsidiary, Bridgeline Digital Pvt. Ltd. located in Bangalore, India.

Liquidity and Management’s Plans

The Company has incurred operating losses and used cash in its operating activities for the past several years. Cash was used to fund operations, develop new products, and build infrastructure. During the past *two* fiscal years and continuing into the current fiscal year, the Company has executed on a restructuring plan that included a reduction of workforce and office space, which significantly reduced operating expenses. The Company is continuing to maintain tight control over discretionary spending in the current fiscal year.

Revenue decreased in the last fiscal year compared to the previous fiscal year and is expected to decline further this fiscal year. The Company has made significant cost reductions over the past few years, but these reductions *may not* be enough to compensate for further declines in revenues in future periods. While there can be *no* assurances that the anticipated sales will be achieved for future periods to provide positive cash flows, the Company's management believes it will have an appropriate cost structure to support the revenues that will be achieved. As such, management believes that it is probable that we will meet our working capital, capital expenditure and debt repayment needs for the next *twelve* months from the financial statement date of issuance.

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 subsidiary. All significant inter-company balances and transactions have been eliminated in consolidation.

Unaudited Interim Financial Information

The unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP"), and with the instructions to Form *10*-Q and Regulation S-*X,* and in the opinion of the Company's management these condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments and accruals, necessary for the fair presentation. The operating results for the *three* months ended *December 31, 2018* are *not* necessarily indicative of the results to be expected for the year ending *September 30, 2019.* The accompanying *September 30, 2018* 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. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form *10*-K for the year ended *September 30, 2018* filed with the Securities and Exchange Commission on *December 28, 2018.*

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

Subsequent Events

The Company evaluated subsequent events through the date of this filing and concluded there were *no* material subsequent events requiring adjustment to or disclosure in these interim condensed consolidated financial statements, except as already disclosed in these financial statements.

Revenue Recognition

In *May 2014,* the Financial Accounting Standards Board (FASB) issued Accounting Standards Update ("ASU") *No. 2014-09,* Revenue from Contracts with Customers: Topic *606* (ASU *2014-09* or ASC *606*), to supersede nearly all existing revenue recognition guidance under U.S. GAAP, which became effective for the Company on *October 1, 2018.* The core principle of ASU *2014-09* is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. ASU *2014-09* defines a *five*-step process to achieve this core principle and, in doing so, it is possible more judgment and estimates *may* be required within the revenue recognition process than required under existing U.S. GAAP including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. Under ASC *606,* revenue is recognized when a customer obtains control of a promised good or service and is recognized in an amount that reflects the consideration that the entity expects to receive in exchange for the good or service. In addition, ASC *606* also includes subtopic ASC *340-40, Other Assets and Deferred Costs- Contracts with Customers*, referred to herein as ASC *340-40,* which provides guidance on accounting for certain revenue related costs including costs associated with obtaining and fulfilling a contract, discussed further below.

The Company adopted the new revenue guidance using the modified retrospective method applied to those contracts which were *not* completed as of *October 1, 2018.* Results for reporting periods beginning after *September 30, 2018* are presented under the new guidance, while prior period amounts are *not* adjusted and continue to be reported in accordance with historic revenue guidance. The Company applied the new standard using practical expedients where:

- the measurement of the transaction price excludes all taxes assessed by governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the Company from a customer;
- the new revenue guidance has been applied to portfolios of contracts with similar characteristics;
- the modified retrospective approach has been applied only to contracts that are *not* completed contracts at the date of initial adoption; and
- the value of unsatisfied performance obligations for contracts with an original expected length of *one* year or less has *not* been disclosed.

Revenue recognition from the Company's primary revenue streams remained substantially unchanged following adoption of ASC *606* and therefore did *not* have a material impact on its revenues. The impact of applying the new guidance in fiscal *2019* versus the prior guidance resulted in a change to the period over which sales commissions are amortized to incorporate an estimated customer life. This resulted in a longer amortization period for deferred commission expense, which reduces expense compared to the application of the prior guidance.

Upon adoption, Other current assets increased by *$50* due to the capitalization of the current portion of sales commissions and other assets increased by *$27* due to the capitalization of the noncurrent portion of sales commissions. Retained earnings increased by *$77* as a net result of these adjustments. The comparative information has *not* been restated and continues to be reported under the accounting standards in effect for those periods.

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

The following tables summarize the impact of adopting ASC *606* on the Company's condensed consolidated financial statements during the *three* months ended and as of *December 31, 2018:*

	As of December 31, 2018		
	As Reported	Adjustments	As If Presented Under ASC 605
Condensed Consolidated Balance Sheet			
Assets			
Other current assets	$ *75*	*50*	$ *25*
Other assets	*232*	*27*	*205*
Equity			
Retained earnings	$ *66,734*	*77*	$ *66,811*

	Three Months Ended December 31, 2018		
	As Reported	Adjustments	As If Presented Under ASC 605
Condensed Consolidated Statement of Operations			
Sales and Marketing	$ *814*	$ *13*	$ *827*
Net loss	$ *(4,955*)	$ *13*	$ *(4,968*)
Net loss per share			
Basic and diluted	$ *(0.46*)	$ *0.01*	$ *(0.45*)

	Three Months Ended December 31, 2018		
	As Reported	**Adjustments**	**As If Presented Under ASC 605**
Condensed Consolidated Statement of Cash Flows			
Cash flows from operating activities			
Net loss	$*(4,955)*	$ *13*	$ *(4,968*)
Other current assets and other assets	$*(10*)	$ *77*	$ *56*

The Company derives its revenue from *three* sources: (i) Software Licenses, which are comprised of subscription fees ("SaaS"), perpetual software licenses, and maintenance for post-customer support ("PCS") on perpetual licenses, (ii) Digital Engagement Services, which are professional services to implement our products such as web development, digital strategy, information architecture and usability engineering and (iii) hosting of perpetual licenses. Customers who license the software on a subscription basis, which can be described as "Software as a Service" or "SaaS" and do *not* take possession of the software.

Revenue is recognized when control of these services is transferred to the Company's customers, in an amount that reflects the consideration the Company expects to be entitled to in exchange for those services. If the consideration promised in a contract includes a variable amount, for example, overage fees, contingent fees or service level penalties, the Company includes an estimate of the amount it expects to receive for the total transaction price if it is probable that a significant reversal of cumulative revenue recognized will *not* occur. The Company's subscription service arrangements are non-cancelable and do *not* contain refund-type provisions. Revenue is reported net of applicable sales and use tax.

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

The Company recognizes revenue from contracts with customers using a *five*-step model, which is described below:

- Identify the customer contract;
- Identify performance obligations that are distinct;
- Determine the transaction price;
- Allocate the transaction price to the distinct performance obligations; and
- Recognize revenue as the performance obligations are satisfied.

Identify the customer contract

A customer contract is generally identified when there is approval and commitment from both the Company and its customer, the rights have been identified, payment terms are identified, the contract has commercial substance and collectability and consideration is probable.

Identify performance obligations that are distinct

A performance obligation is a promise to provide a distinct good or service or a series of distinct goods or services. A good or service that is promised to a customer is distinct if the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer, and a company's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract.

Determine the transaction price

The transaction price is the amount of consideration to which the Company expects to be entitled in exchange for transferring goods or services to a customer, excluding sales taxes that are collected on behalf of government agencies.

Allocate the transaction price to the distinct performance obligations

The transaction price is allocated to each performance obligation based on the relative standalone selling prices ("SSP") of the goods or services being provided to the customer. The Company determines the SSP of its goods and services based upon the historical average sales prices for each type of software license and professional services sold.

Recognize revenue as the performance obligations are satisfied

Revenues are recognized when or as control of the promised goods or services is transferred to customers. Revenue from SaaS licenses is recognized ratably over the subscription period beginning on the date the license is made available to customers. Most subscription contracts are *three*-year terms. Customers who license the software on a perpetual basis receive rights to use the software for an indefinite time period and an option to purchase post-customer support ("PCS"). PCS revenue is recognized ratably on a straight-line basis over the period of performance and the perpetual license is recognized upon delivery. The Company also offers hosting services for those customers who purchase a perpetual license and do *not* want to run the software in their environment. Revenue from hosting is recognized ratably over the service period, ranging from *one* to *three*-year terms. The Company recognizes revenue from professional services as the services are provided.

Disaggregation of Revenue

The Company provides disaggregation of revenue based on geography and product groupings within the notes (Note *11*) as it believes this best depicts how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

Deferred Revenue

Amounts that have been invoiced are recorded in accounts receivable and deferred revenue or revenue, depending on whether the revenue recognition criteria have been met. Deferred revenue represents amounts billed for which revenue has *not* yet been recognized. Deferred revenue that will be recognized during the succeeding *12*-month period is recorded as current deferred revenue, and the remaining portion is recorded as noncurrent deferred revenue included in Other long term liabilities. Deferred revenue during the *three* months ended *December 31, 2018* increased by *$341.* As of *December 31, 2018,* approximately *$13* of revenue is expected to be recognized from remaining performance obligations for contracts with original performance obligations that exceed *one* year. The Company expects to recognize revenue on approximately *99%* of these remaining performance obligations over the next *24* months, with the balance recognized thereafter.

	Deferred Revenue	
	Current	**Noncurrent**
Balance as of October 1, 2018	$ *594*	$ *20*
Increase(decrease)	$ *341*	$ *(7*)
Balance as of December 31, 2018	$ *935*	$ *13*

Deferred Capitalized Commission Costs

The incremental direct costs of obtaining a contract, which primarily consist of sales commissions paid for new subscription contracts, are deferred and amortized on a straight-line basis over a period of approximately *three* years. The Company evaluated both qualitative and quantitative factors, including the estimated life cycles of its offerings, renewal rates, and its customer attrition to determine the amortization periods for the capitalized costs. The initial amortization period will generally be the customer contract term, which is typically *thirty-six* (*36*) months, with some exceptions. Deferred capitalized commission expense that will be recorded as expense during the succeeding *12*-month period is recorded as current deferred capitalized commission costs, and the remaining portion is recorded as long-term deferred capitalized commission costs. Deferred capitalized commissions increased by *$29* for the quarter ended *December 31, 2018* compared to *$77* for the year ended *September 30, 2018.* Current deferred capitalized commission costs are included in Other current assets in the Condensed Consolidated Balance Sheet and noncurrent deferred capitalized commission costs are included in Other assets in the Condensed Consolidated Balance Sheet. Amortization expense for the *three* months ended *December 31, 2018* was *$15.*

Accounting Pronouncements Pending Adoption

Leases

In *February 2016,* the FASB issued ASU *No. 2016-02,* which is guidance on accounting for leases. ASU *No. 2016-02* requires lessees to recognize most leases on their balance sheets for the rights and obligations created by those leases. The guidance requires enhanced disclosures regarding the amount, timing, and uncertainty of cash flows arising from leases and will be effective for interim and annual periods beginning after *December 15, 2018.* Early adoption is permitted. The guidance requires the use of a modified retrospective approach. The Company is evaluating the impact of the guidance on its consolidated financial position, results of operations and related disclosures.

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

Earnings Per Share

In *July 2017,* the FASB issued ASU *No. 2017-11,* which simplifies the accounting for certain financial instruments with down round features. This new standard will reduce income statement volatility for many companies that issue warrants and convertible instruments containing such features. ASU *2017-11* is effective for public companies in *2019* and all other entities in *2020.* Management is currently evaluating the impact of the new guidance on its consolidated financial statements.

Compensation – Stock Compensation

In *June 2018,* the FASB issued ASU *2018-07,* which expands the scope of Topic *718* to include share-based payment transactions for acquiring goods and services from nonemployees. ASU *2018-07* is effective for interim periods in fiscal years beginning after *December 15, 2018,* with early adoption permitted, but *no* earlier than the Company's adoption date of Topic *606.* The new guidance is required to be applied retrospectively with the cumulative effect recognized at the date of initial application. Management is currently evaluating the impact of the new guidance on its consolidated financial statements.

Intangibles – Goodwill and Other - Internal-Use Software

In *August 2018,* the FASB issued ASU *2018-15,* which addresses a customer's accounting for implementation costs incurred in a cloud computing arrangement that is a service contract. Under the new guidance, customers will apply the same criteria for capitalizing implementation costs as they would for an arrangement that has a software license. ASU *2018-15* is effective for interim periods in fiscal years beginning after *December 15, 2019,* with early adoption permitted.

Fair Value

In *August 2018,* the FASB issued ASU *2018-13,* which is guidance that changes the fair value measurement disclosure requirements of ASC *820.* This guidance is will be effective for all entities for fiscal years beginning after *December 15, 2019,* including interim periods therein. Early adoption is permitted for any eliminated or modified disclosures upon issuance of this ASU. The Company is evaluating the impact the update will have on its disclosures.

All other Accounting Standards Updates issued but *not* yet effective are *not* expected to have a material effect on the Company's future financial statements.

BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

3. Accounts Receivable and Unbilled Receivables

Accounts receivable and unbilled receivables consists of the following:

	As of December 31, 2018	As of September 30, 2018
Accounts receivable	$ *2,332*	$ *1,866*
Unbilled receivables	*98*	*36*
Subtotal	*2,430*	*1,902*
Allowance for doubtful accounts	*(163*)	*(181*)
Accounts receivable and unbilled receivables, net	$ *2,267*	$ *1,721*

For the *three* months ended *December 31, 2018, three* customers represented more than *10%* of accounts receivable. For the year ended *September 30, 2018, two* customers represented more than *10%* of accounts receivable. For the *three* months ended *December 31, 2018, two* customers represented *18%* and *19%* of the Company’s total revenue. For the year ended *September 30, 2018, three* customers each represented approximately *10% - 14%* of the Company’s total revenue.

4. Fair Value Measurement and Fair Value of Financial Instruments

The Company's other financial instruments consist principally of accounts receivable, accounts payable, and debt. The Company measures its financial assets and liabilities at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., exit price) in an orderly transaction between market participants at the measurement date. Additionally, companies are required to provide disclosure and categorize assets and liabilities measured at fair value into *one* of *three* different levels depending on the assumptions (i.e., inputs) used in the valuation. Level *1* provides the most reliable measure of fair value while Level *3* generally requires significant management judgment. Financial assets and liabilities are classified in their entirety based on the lowest level of input significant to the fair value measurement. The fair value hierarchy is defined as follows:

Level *1—Valuations* are based on unadjusted quoted prices in active markets for identical assets or liabilities.

Level *2—Valuations* are based on quoted prices for similar assets or liabilities in active markets, or quoted prices in markets that are *not* active for which significant inputs are observable, either directly or indirectly.

Level *3—Valuations* are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. Inputs reflect management's best estimate of what market participants would use in valuing the asset or liability at the measurement date.

The Company believes the recorded values for accounts receivable and accounts payable and short term debt approximate current fair values as of *December 31, 2018* and *September 30, 2018* because of their short-term nature and durations. The carrying value of long term debt also approximates fair value as of *December 31, 2018* and *September 30, 2018* based upon the Company's ability to acquire similar debt at similar maturities and renew current debt instruments under similar terms as the original debt.

In *October 2017,* the Company recorded a liability associated with a warrant to purchase common stock issued to Montage Capital II, L.P ("Montage Capital"). The fair value of the warrant liability utilizes a Level *3* input. To determine the value of the warrant liability, the Company used a Monte Carlo option-pricing model, which takes into consideration the market values of comparable public companies, considering among other factors, the use of multiples of earnings, and adjusted to reflect the restrictions on the ability of our shares to trade in an active market. The Monte Carlo option-valuation model also uses certain assumptions to determine the fair value, including expected life and annual volatility. The initial valuation assumptions included an expected life of *eight* (*8*) years, annual volatility of *80%,* and a risk-free interest rate of *2.24%.* At *December 31, 2018,* annual volatility decreased to *74%,* the risk-free rate was *2.58%* and the Company's stock price declined to *$0.23* per share.

The fair value of the warrant liability was valued at the loan execution date in the amount of *$341* and is revalued at the end of each reporting period to fair value. The fair value of the warrant is included in Other long-term liabilities in the Condensed Consolidated Balance Sheet. Changes in fair value are included in interest expense in the Statement of Operations in the period the change occurs. In total, the Company has recorded a change in fair value of *$173* since the original valuation in *October 2017.* The fair value of the warrant at *December 31, 2018* is *$168.*

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BRIDGELINE DIGITAL, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share and per share data)

Assets and liabilities of the Company measured at fair value on a recurring basis as of *December 31, 2018* and *September 30, 2018* are as follows:

	As of December 31, 2018			
	Level 1	**Level 2**	**Level 3**	**Total**
Liabilities:				
Warrant liability	$ -	$ -	$ *168*	$ *168*
Total Liabilities	$ -	$ -	$ *168*	$ *168*

	As of September 30, 2018			
	Level 1	**Level 2**	**Level 3**	**Total**
Liabilities:				
Warrant liability	$ -	$ -	$ *180*	$ *180*
Total Liabilities	$ -	$ -	$ *180*	$ *180*

The following table provides a rollforward of the fair value, as determined by Level *3* inputs, of the warrant liability.

Warrant Liability

	Three Months Ended December 31, 2018
Balance at beginning of period, October 1, 2018	$ *180*
Adjustment to fair value	*(12*)
Balance at end of period, December 31, 2018	$ *168*

5. Goodwill

The carrying value of goodwill is *not* amortized, but is typically tested for impairment annually as of *September 30,* as well as, whenever events or changes in circumstances indicate that the carrying amount of a reporting unit *may not* be recoverable. The purpose of an impairment test is to identify any potential impairment by comparing the carrying value of a reporting unit including goodwill to its fair value. An impairment charge is recognized for the amount by which the carrying amount exceeds the reporting unit's fair value, however, the loss recognized should *not* exceed the total amount of goodwill allocated to that reporting unit.

BRIDGELINE DIGITAL, INC.

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An interim test was performed at *December 31, 2018,* as a decline in the stock price and other negative qualitative factors led management to conclude that there was a potential impairment. The fair value was calculated using the Company's market price. In performing the interim impairment test, Management concluded that goodwill was impaired and recorded a charge of *$3.7* million. This amount is reflected as a reduction in goodwill of *$3.7* million in the Company's Condensed Consolidated Balance Sheet as of *December 31, 2018* with the offset as an expense in the Company's Condensed Consolidated Statement of Operations.

Changes in the carrying value of goodwill are as follows:

	As of December 31, 2018	**As of September 30, 2018**
Balance at beginning of period	$ *7,782*	$ *12,641*
Impairment	*(3,732*)	*(4,859*)
Balance at end of period	$ *4,050*	$ *7,782*

6. **Intangible Assets**

The components of intangible assets, net of accumulated amortization, are as follows:

	As of December 31, 2018	As of September 30, 2018
Domain and trade names	$ *10*	$ *10*
Non-compete agreements	*7*	*10*
	$ *17*	$ *20*

Total amortization expense related to intangible assets for the *three* months ended *December 31, 2018* and the year ended *September 30, 2018* was *$4* and *$242,* respectively, and is reflected in operating expenses on the Condensed Consolidated Statements of Operations. The estimated amortization expense for fiscal year *2019* (remaining) and *2020* is *$7* and *$0,* respectively.

7. Restructuring

Commencing in fiscal *2015* and through fiscal *2017,* the Company's management approved, committed to and initiated plans to restructure and further improve efficiencies by implementing cost reductions in line with expected decreases in revenue. The Company renegotiated several office leases and relocated to smaller space, while also negotiating sub-leases for the original space. In addition, the Company executed a general work-force reduction and recognized costs for severance and termination benefits. These restructuring charges and accruals require estimates and assumptions, including contractual rental commitments or lease buy-outs for vacated office space and related costs, and estimated sub-lease income. The Company's sub-lease assumptions include the rates to be charged to a sub-tenant and the timing of the sub-lease arrangement. All of the vacated lease spaces are currently contractually occupied by new sub-tenants for the remaining life of the lease. In the *second* quarter of fiscal *2017,* the Company initiated a plan to shut down its operations in India, which is targeted to be completed in early fiscal *2019.* All of these estimates and assumptions will be monitored on a quarterly basis for changes in circumstances with the corresponding adjustments reflected in the consolidated statement of operations. All of these estimates and assumptions will be monitored on a quarterly basis for changes in circumstances with the corresponding adjustments reflected in the Condensed Consolidated Statement of Operations.

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The following table summarizes the restructuring activity for the *three* months ended *December 31, 2018:*

	Facility Closures and Other Costs
Balance at beginning of period, October 1, 2018	$ *78*
Charges to operations	-
Cash disbursements	*(29*)
Changes in estimates	-
Balance at end of period, December 31, 2018	$ *49*

The components of the accrued restructuring liabilities is as follows:

	As of December 31, 2018	**As of September 30, 2018**
Facilities and related	$ *49*	$ *77*
Other	-	*1*
Total	$ *49*	$ *78*

As of *December 31, 2018, $37* was reflected in Accrued Liabilities and *$12* in Other Long-Term Liabilities in the Condensed Consolidated Balance Sheet. As of *September 30, 2018, $53* is reflected in Accrued Liabilities and *$25* is reflected in Other Long-Term Liabilities in the Condensed Consolidated Balance Sheet.

8. Debt

The Company's debt as of *December 31, 2018,* consisted of the Line of Credit from Heritage Bank of Commerce ("Heritage Bank") and a term loan with Montage Capital II, L.P. *(* "Montage Capital"). The Company's debt as of *September 30, 2018,* consisted of the Line of Credit from Heritage Bank, a term loan with Montage Capital, and Promissory Term Notes.

Debt at *December 31, 2018* and *September 30, 2018* consists of the following:

	As of December 31, 2018	**As of September 30, 2018**
Line of credit borrowings	$ *1,880*	$ *2,081*
Term loan - Montage Capital	*844*	*922*
Other promissory notes	-	*941*
Other (debt discount)	*(203*)	*(353*)
Total debt	$ *2,521*	$ *3,591*
Less current portion	$ *198*	$ *1,017*
Long term debt, net of current portion	$ *2,323*	$ *2,574*

BRIDGELINE DIGITAL, INC.

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Heritage Line of Credit

In *June 2016,* the Company entered into a new Loan and Security Agreement ("Heritage Agreement"), with Heritage Bank. The Heritage Agreement had an original a term of *24* months but was further amended in *February 2019* to a maturity date of *February 29, 2020.* The Company paid an annual commitment fee of *0.4%* of the commitment amount in the *first* year and *0.2%* in the following years. The facility fee will be *$6* on each anniversary thereafter. Borrowings are secured by all of the Company's assets and all of the Company's intellectual property. The Company is required to comply with certain financial and reporting covenants including an Asset Coverage Ratio and an Adjusted EBITDA metric. The Company was in compliance with all financial covenants as of *December 31, 2018.*

The Heritage Agreement provides for up to *$2.5* million of revolving credit advances which *may* be used for acquisitions and working capital purposes. Borrowings are limited to the lesser of (i) *$2.5* million and (ii) *75%* of eligible receivables as defined. The Company can borrow up to *$1.0* million in out of formula borrowings for specified periods of time. The borrowings or credit advances *may not* exceed the monthly borrowing base capacity, which will fluctuate based on monthly accounts receivable balances. The Company *may* request credit advances if the borrowing capacity is more than the current outstanding loan advance, and must pay down the outstanding loan advance if it exceeds the borrowing capacity. Borrowings accrue interest at Wall Street Journal Prime Rate plus *1.75%,* (*7.25%* and *7.0%* at *December 31, 2018* and *September 30, 2018,* respectively). As of *December 31, 2018,* the Company had an outstanding balance under the Heritage Agreement of *$1.9* million and additional borrowing capacity of *$200.*

Amendments – Heritage Bank

The Company and Heritage Bank have executed numerous amendments since the origination of the Heritage Agreement. Those amendments that are relevant as of *December 31, 2018* are the following:

The *first* amendment, executed on *August 15, 2016,* included a decrease in the revolving line of credit from *$3.0* million to *$2.5* million. The *second* amendment, executed on *December 14, 2016,* included a minimum cash requirement of *$250* in the Company's accounts at Heritage. On *October 6, 2017,* a *fourth* amendment was executed, which included a consent to the Company's incurrence of additional indebtedness from Montage Capital and the grant of a *second* position lien to Montage Capital. In addition, Heritage Bank and Montage Capital entered into an Intercreditor Agreement dated *October 10, 2017* and acknowledged by the Company. On *September 21, 2018,* the *ninth* amendment was executed and addressed the minimum unrestricted cash requirements for the Company's accounts at Heritage Bank upon repayment of certain Promissory Term Notes issued by the Company on *September 7, 2018* in the principal amount of *$941.* On *December 27, 2018,* the *tenth* amendment was executed, which extended the maturity date of the Loan Agreement to *January 1, 2020,* as well as, set new financial covenants for fiscal *2019.* On February *14, 2019,* the *eleventh* amendment was executed, which extended the maturity date of the Loan Agreement to February *29, 2020,* as well as, set new financial covenants for fiscal *2019.*

Montage Capital II, L.P. Loan Agreement

On *October 10, 2017,* the Company entered into a Loan and Security Agreement (the "Montage Agreement or Montage Loan") with Montage Capital. The Montage Agreement has a *thirty-six* (*36*) month term which matures on *October 10, 2020.* The Montage Agreement provided for up to *$1.5* million of borrowing in the form of a non-revolving term loan which *may* be used by the Company for working capital purposes. *$1* million of borrowing was advanced on the date of closing and the option to borrow the remainder has lapsed. Borrowings bear interest at the rate of *12.75%* per annum. The Company paid a fee of *$47* to Montage Capital at closing. Interest only payments are due and payable during the *first nine* months of the Montage Loan. On *July 1, 2018,* the Company commenced payment of principal payments of *$26* per month plus accrued interest. All remaining principal and interest shall be due and payable at maturity. Borrowings are secured by a *second* position lien on all of the Company's assets including intellectual property and general intangibles and is subordinate to the Company's senior debt facility with Heritage Bank. Pursuant to the Montage Agreement, the Company is also required to comply with certain financial covenants.

On *May 10, 2018,* the *first* amendment to the Montage Agreement (the "First Amendment") was executed. The First Amendment included the Adjusted EBITDA metrics for the *third* quarter of fiscal *2018* and a waiver for *not* achieving the Adjusted EBITDA metrics for the quarter ended *March 31, 2018.* A *second* amendment to the Montage Agreement (the "Second Amendment") was executed on *October 22, 2018.* The Second Amendment included modifications to financial covenants and addressed the minimum unrestricted cash requirements for the Company's accounts at Heritage Bank upon repayment of debt incurred by the Company pursuant to certain Promissory Term Notes (see below) issued by the Company on *September 7, 2018* in the principal amount of *$941.* A *third* amendment to the Montage Agreement (the "Third Amendment") was executed on *December 7, 2018* and included the new financial covenants for fiscal *2019.* The Company was in compliance with all financial covenants as of *December 31, 2018.*

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As additional consideration for the Montage Loan, the Company issued to Montage Capital an *eight*-year warrant (the "*Montage Warrant*") to purchase *66,315* shares of the Company's common stock at a price equal to *$2.65* per share. The Montage Warrant contains an equity buy-out provision upon the earlier of (*1*) dissolution or liquidation of the Company, (*2*) any sale or distribution of all or substantially all of the assets of the Company or (*3*) a "Change in Control" as defined within the meaning of Section *13*(d) and *14*(d)(*2*) of the Securities Exchange Act of *1934.* Montage Capital shall have the right to receive an equity buy-out of *$250.* If the equity buy-out is exercised, the Montage Warrant will be surrendered to the Company for cancellation.

Promissory Term Notes

On *September 7, 2018,* the Company sold and issued subordinate promissory notes (the "*Promissory Term Notes*") to certain accredited investors ("Purchasers"), pursuant to which it issued to the Purchasers (i) Promissory Term Notes, in the aggregate principal amount of approximately *$941.* The Promissory Term Notes have an original issue discount of *fifteen* percent (*15%*), bear interest at a rate of *twelve* percent (*12%*) per annum, and have a maturity date of the earlier to occur of (a) *six* months from the date of execution of the Purchase Agreement, or (b) the consummation of a debt or equity financing resulting in the gross proceeds to the Company of at least *$3.0* million. After recording *$141* of original issue discount and debt issuance costs of *$40,* the Company received net cash proceeds in the aggregate amount of *$760* for the Promissory Term Notes. The original issue discount and debt issuance costs are recorded as a contra liability and will be amortized over the life of the Promissory Term Notes. On *October 19, 2018,* the Company completed an equity financing resulting in gross proceeds of *$5.0* million and repaid the Promissory Term Notes including accrued interest of *$13* for a total of *$954* on *October 23, 2018.* Such repayments were approved by both Heritage Bank and Montage Capital.

Further, Heritage Bank and Montage Capital, both approved the issuance of the Promissory Term Notes and the repayment terms and each Purchaser also entered into a Subordination Agreement with the *two* parties, pursuant to which the Purchasers agreed to subordinate (i) all of the Company's indebtedness and obligations to the Purchasers, whether presently existing or arising in the future, to all of the Company's indebtedness the both Heritage Bank and Montage Capital and (ii) all of the Purchasers' security interests, if any, to all of Heritage Bank's and Montage Capital's security interests in property of the Company.

9. **Shareholders' Equity**

Preferred Stock Series A Convertible

In *October 2014,* the Company designated *264,000* shares of its Preferred stock (the "Preferred Stock") as Series A convertible preferred stock and sold *200,000* shares of Series A convertible preferred stock at a purchase price of *$10.00* per share for gross proceeds of *$2.0* million in a private placement. The shares of Preferred Stock *may* be converted, at the option of the holder at any time, into such number of shares of common stock ("Conversion Shares") equal (i) to the number of shares of Preferred Stock to be converted, multiplied by the stated value of *$10.00* (the "Stated Value") and (ii) divided by the conversion price in effect at the time of conversion. The current conversion price is *$16.25* and is subject to adjustment in the event of stock splits or stock dividends. As of *December 31, 2018,* a total of *1,636* preferred shares have been converted to *1,007* shares of common stock.

Any accrued but unpaid dividends on the shares of Preferred Stock to be converted shall also be converted in common stock at the conversion price. A mandatory provision also *may* provide that the Company will have the right to require the holders to convert shares of Preferred Stock into Conversion Shares if (i) the Company's common stock has closed at or above *$32.50* per share for *ten* consecutive trading days and (ii) the Conversion Shares are (A) registered for resale on an effective registration statement or (B) *may* be resold pursuant to Rule *144.*

In the event of any liquidation, dissolution, or winding up of the Company, the holders of shares of Preferred Stock will be entitled to receive in preference to the holders of common stock, the amount equal to the stated value per share of Series A Preferred Stock plus declared and unpaid dividends, if any. After such payment has been made, the remaining assets of the Company will be distributed ratably to the holders of common stock. The Preferred Shares shall vote with the Common Stock on an as converted basis.

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Effective *January 1, 2017,* cumulative dividends are payable at a rate of *12%* per year. The Company has issued *64,000* shares of Preferred Stock as PIK dividends to the preferred shareholders, which is the maximum amount of cumulative PIK dividends authorized. Therefore, all future dividend payments will be cash dividends. Total cash dividend payments for the *three* months ended *December 31, 2018* were *$79.*

Preferred Stock Series B Convertible

On *October 16, 2018,* in connection with a public offering, the Company issued *4,288* Series B Convertible Preferred Stock, par value *$0.001* per share, with each share of Series B Convertible Preferred Stock convertible into *2,000* shares of the Company's common stock at a conversion price of *$0.50* per share. As of *December 31, 2018, 4,208* shares of Series B Convertible Preferred Stock have been converted into *8,416,000* shares of common stock.

Common Stock

Public Offering

On *October 16, 2018,* the Company issued and sold in a public offering (the "*Offering*") an aggregate of (i) *1,424,000* Class A Units (the "Class A Units") at a price of *$0.50* per Class A Unit, consisting of (i) *one* share of the Company's common stock and *one five*-year warrant to purchase *one* share of Company common stock at an exercise price of *$0.50* per share and (ii) *4,288* Class B Units, consisting of *one* share of Series B Convertible Preferred Stock and a Warrant to purchase *one* share of common stock. Each share of Series B Convertible Preferred Stock is convertible into *2,000* shares of the Company's common stock at a conversion price of *$0.50* per share. The net proceeds to the Company from the Offering, after deducting the underwriter's fees and expenses, the Company's Offering expenses and the repayment of the Promissory Term Notes were approximately *$3.4* million.

In addition, the Company granted the underwriter of the Offering a *45*-day option (the "*Over-allotment Option")* to purchase up to an additional *1.5* million shares of common stock and additional warrants to purchase an additional *1.5* million shares of common stock. At the time of the Offering, the underwriter partially exercised the Over-allotment Option by electing to purchase from the Company additional warrants to purchase *400,000* shares of common stock.

Amended and Restated Stock Incentive Plan

The Company has granted common stock, common stock warrants, and common stock option awards (the "Equity Awards") to employees, consultants, advisors and debt holders of the Company and to former owners and employees of acquired companies that have become employees of the Company. On *April 29, 2016,* the stockholders approved a new stock incentive plan, The *2016* Stock Incentive Plan (the *"2016* Plan"). The *2016* Plan replaced an older plan that had expired in *August 2016.* The *2016* Plan authorizes the award of incentive stock options, non-statutory stock options, restricted stock, unrestricted stock, performance shares, stock appreciation rights and any combination thereof to employees, officers, directors, consultants, independent contractors and advisors of the Company. Initially, a total of *500,000* shares of the Company's Common Stock is reserved for issuance under the *2016* Plan. As of *December 31, 2018,* there were *232,066* options outstanding under this plan and *267,934* shares available for future issuance.

BRIDGELINE DIGITAL, INC.

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Common Stock Warrants

The Company typically issues warrants to individual investors and placement agents to purchase shares of the Company's common stock in connection with public and private placement fund raising activities. Warrants *may* also be issued to individuals or companies in exchange for services provided for the Company. The warrants are typically exercisable *six* months after the issue date, expire in *five* years, and contain a cashless exercise provision and piggyback registration rights.

Total warrants outstanding as *December 31, 2018* were as follows:

Type	**Issue Date**	**Shares**	**Price**	**Expiration**
Placement Agent	3/28/2014	*12,800*	$*26.25*	3/28/2019
Placement Agent	10/28/2014	*12,308*	$*16.25*	10/28/2019
Director/Shareholder	12/31/2014	*12,000*	$*20.00*	12/31/2019
Director/Shareholder	2/12/2015	*12,000*	$*20.00*	2/12/2020
Director/Shareholder	5/12/2015	*12,000*	$*20.00*	5/12/2020
Director/Shareholder	12/31/2015	*6,000*	$*20.00*	12/31/2020
Placement Agent	5/17/2016	*86,778*	$*3.75*	5/17/2021
Placement Agent	5/11/2016	*53,334*	$*3.75*	5/11/2021
Placement Agent	7/15/2016	*44,000*	$*4.60*	7/15/2021
Investors	11/9/2016	*213,538*	$*3.50*	5/22/2022
Director/Shareholder	12/31/2016	*6,000*	$*20.00*	12/31/2021
Financing	10/10/2017	*66,315*	$*2.65*	10/10/2025
Director/Shareholder	12/31/2017	*6,000*	$*20.00*	12/31/2022
Investors	10/19/2018	*10,400,000*	$*0.50*	10/19/2023
Placement Agent	10/19/2018	*500,000*	$*0.625*	10/16/2023
Total		*11,443,073*		

Summary of Option and Warrant Activity and Outstanding Shares

	Stock Options		Stock Warrants	
	Options	Weighted Average Exercise Price	Warrants	Weighted Average Exercise Price
Outstanding, October 1, 2018	*457,846*	$ *6.83*	*546,151*	$ *6.16*
Granted	-	$ -	*10,900,000*	$ *0.51*
Exercised	-	$ -	-	$ -
Forfeited or expired	*(14,068*)	$ *(24.58*)	*(3,078*)	$ *(32.50*)
Outstanding, December 31, 2018	*443,778*	$ *6.52*	*11,443,073*	$ *0.77*

BRIDGELINE DIGITAL, INC.

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	Three Months Ended December 31,	
	2018	**2017**
Number of options granted	*none*	*800*
Volatility	*n/a*	*83.45%*
Estimated life (in years)	*n/a*	*6*
Risk-free interest rate	*n/a*	*2.02 %*
Weighted-average fair value per share of grants	*n/a*	$*2.92*

10. Net Loss Per Share

Basic and diluted net loss per share is computed as follows:

(in thousands, except per share data)	**Three Months Ended December 31,**	
	2018	**2017**
Net loss	$*(4,955*)	$*(430*)
Accrued dividends on convertible preferred stock	*(79*)	*(75*)
Net loss applicable to common shareholders	$*(5,034*)	$*(505*)
Weighted average common shares outstanding - basic and diluted	*11,008*	*4,200*

Net loss per share attributable to common shareholders:

Basic and diluted	$*(0.46*)	$*(0.12*)

Basic net loss per share is computed by dividing net loss available to common shareholders by the weighted average number of common shares outstanding. Diluted net income per share is computed using the weighted average number of common shares outstanding during the period plus the dilutive effect of outstanding stock options and warrants and convertible preferred stock using the "treasury stock" method. For both the *three* months ended *December 31, 2018* and *2017,* the computation of diluted loss per share does *not* include all of stock options, warrants and convertible preferred stock as they are anti-dilutive.

11. **Disaggregated Revenue and Segment Reporting**

The Company operates as *one* operating segment, therefore, all required financial segment information can be found in the condensed consolidated financial statements.

The Company disaggregates revenue from contracts with customers by geography and product grouping, as it believes this best depicts how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

BRIDGELINE DIGITAL, INC.

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(in thousands, except share and per share data)

The Company's revenue by geography (based on customer address) is as follows:

	Three Months Ended December 31,	
Revenues:	**2018**	**2017**
United States	$*2,353*	$*3,862*
International	$*22*	$*107*
	$*2,375*	$*3,969*

The Company's revenue by type is as follows:

	Three Months Ended December 31,	
Revenues:	**2018**	**2017**
Digital Engagement Services	$*1,073*	$*2,060*
Subscription	*764*	*1,477*
Perpetual Licenses	*154*	-
Maintenance	*127*	*129*
Hosting	*257*	*303*
	$*2,375*	$*3,969*

***12*. Income Taxes**

Income tax expense was *$4* and *$1* for the *three* months ended *December 31, 2018* and *2017.* Income tax expense consists of the estimated liability for federal and state income taxes owed by the Company, including the alternative minimum tax. Net operating loss carry forwards are estimated to be sufficient to offset any potential taxable income for all periods presented.

***13*. Related Party Transactions**

In *November 2018,* the Company engaged Taglich Brothers Inc,,on a non-exclusive basis, to perform advisory and investment banking services with possible acquisition target possibilities. Michael Taglich, a director and shareholder of the Company, is the President and Chairman of Taglich Brothers Inc.   Fees for the services are *$8* per month for *three* months and *$5* thereafter, cancellable at any time. Taglich Brothers Inc. *may* also earn a success fee ranging from *$200* for a revenue target acquisition of under *$5* million up to *$1* million for an acquisition target over *$200* million.

***14*. Legal Proceedings**

The Company is subject to ordinary routine litigation and claims incidental to its business. As of *December 31, 2018,* the Company was *not* engaged with any material legal proceedings.

***15.* Subsequent Events**

On *February 13, 2019,* the Company entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Seevolution Inc, a Delaware corporation, Celebros, Inc., a Delaware corporation, and Elisha Gilboa,an individual and shareholder of Seevolution, collectively (the “Sellers”). The Asset Purchase Agreement sets forth the terms and conditions pursuant to which the Company acquired certain assets of the Sellers in exchange for consideration paid to the Sellers consisting of (i) *$400,000* in cash, (ii) the payment of *$100,000* of additional cash to be paid out *$10,000* per month for *ten* months starting *April 30, 2019* and (iii) *2,000,000* shares of Bridgeline Digital common stock.

On *February 14, 2019,* the Company paid a deposit of *$498* to secure a bid and commence confirmatory due diligence related to the potential acquisition of a Canadian company that filed a Notice of Intention to File a Proposal under the Bankruptcy and Insolvency Act. Due to the terms of the sale and investment solicitation process (bid process), the name of the acquisition target cannot be revealed until the confirmatory due diligence is completed and the Canadian court approves the sale, which will be at the end of *February 2019.*

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

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

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

Overview

Bridgeline Digital, The Digital Engagement Company™, helps customers maximize the performance of their full digital experience from websites and intranets to eCommerce experiences. Bridgeline's Unbound platform is a Digital Experience Platform that deeply integrates Web Content Management, eCommerce, eMarketing, Social Media management, and Web Analytics (Insights) with the goal of assisting marketers to deliver exceptional digital experiences that attract, engage, nurture and convert their customers across all channels. Bridgeline offers a core accelerator framework for rapidly implementing digital experiences on the Bridgeline Unbound Platform which provides customers with cost-effective solutions in addition to velocity to market.

Bridgeline's Unbound platform combined with its professional services assists customers in digital business transformation, driving lead generation, increasing revenue, improving customer service and loyalty, enhancing employee knowledge, and reducing operational costs. The Bridgeline Unbound platform bridges the gaps between web content management, eCommerce, eMarketing, social and web analytics by providing all of these components in one unified and deeply integrated platform.

Our Unbound Franchise product empowers large franchises, healthcare networks, associations/chapters and other multi-unit organizations to manage a large hierarchy of digital properties at scale. The platform provides an easy-to-use administrative console that enables corporate marketing to provide consistency in branding and messaging while providing flexible publishing capabilities at the local-market level. The platform empowers brand networks to unify, manage, scale and optimize a hierarchy of web properties and marketing campaigns on a global, national and local level.

The Unbound platform is delivered through a cloud-based software as a service ("*SaaS*") 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 software resides on a dedicated infrastructure in either the customer's facility or manage-hosted by Bridgeline via a cloud-based hosted services model.

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 has one wholly-owned subsidiary, Bridgeline Digital Pvt. Ltd. located in Bangalore, India.

Customer Information

For the three months ended December 31, 2018, two customers represented 18% and 19% of the Company's total revenue. For the three months ended December 31, 2017, two customers represented 11% and 12% of the Company's total revenue.

Results of Operations for the Three Months Ended December 31, 2018 compared to the Three Months Ended December 31, 2017

Total revenue for the three months ended December 31, 2018 was $2.4 million and $4.0 million for the three months ended December 31, 2017. We had a net loss of ($5.0) million for the three months ended December 31, 2018 and ($430) thousand for the three months ended December 31, 2017. Included in the net loss for the three months ending December 31, 2018 was a goodwill impairment of $3.7 million. Net loss per share applicable to common shareholders was ($0.46) for the three months ended December 31, 2018 and ($0.12) for the three months ended December 31, 2017.

(in thousands)	**Three Months Ended December 31, 2018**		**Three Months Ended December 31, 2017**		**$ Change**	**% Change**
Revenue						
Digital engagement services	$ 1,073		$ 2,060		$ (987)	(48 %)
% of total revenue	45	%	52	%		
Subscription and perpetual licenses	1,045		1,606		(561)	(35 %)
% of total revenue	44	%	40	%		
Managed service hosting	257		303		(46)	(15 %)
% of total revenue	11	%	8	%		
Total revenue	**2,375**		**3,969**		**(1,594)**	**(40 %)**
Cost of revenue						
Digital engagement services	855		1,397		(542)	(39 %)
% of digital engagement revenue	80	%	68	%		
Subscription and perpetual licenses	423		480		(57)	(12 %)
% of subscription and perpetual licenses revenue	40	%	30	%		
Managed service hosting	63		80		(17)	(21 %)
% of managed service hosting	25	%	26	%		
Total cost of revenue	1,341		1,957		(616)	(31 %)
Gross profit	**1,034**		**2,012**		**(978)**	**(49 %)**
Gross profit margin	**44**	**%**	**51**	**%**		
Operating expenses						
Sales and marketing	814		1,030		(216)	(21 %)
% of total revenue	34	%	26	%		
Support	91		74		17	23 %
% of total revenue	4	%	2	%		
General and administrative	687		736		(49)	(7 %)
% of total revenue	29	%	19	%		

Research and development	418		407		11		3	%
% of total revenue	18	%	10	%				
Depreciation and amortization	26		108		(82	)	(76	%)
% of total revenue	1	%	3	%				
Goodwill impairment	3,732		-		3,732		100	%
% of total revenue	157	%	0	%				
Total operating expenses	**5,768**		**2,355**		**3,413**		**145**	**%**
% of total revenue	243	%	59	%				
Loss from operations	(4,734	)	(343	)	(4,391	)	1,280	%
Interest and other expense, net	(217	)	(86	)	(131	)	152	%
Loss before income taxes	(4,951	)	(429	)	(4,522	)	1,054	%
Provision for income taxes	4		1		3		300	%
Net loss	**$ (4,955**	**)**	**$ (430**	**)**	**$ (4,525**	**)**	**1,052**	**%**
Non-GAAP Measure								
Adjusted EBITDA	**$ (866**	**)**	**$ (94**	**)**	**$ (772**	**)**	**821**	**%**

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Revenue

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

Digital Engagement Services

Digital engagement services revenue is comprised of Bridgeline Unbound implementation and retainer related services. In total, revenue from digital engagement services decreased $987 thousand, or 48%, to $1.1 million for the three months ended December 31, 2018 compared to $2.1 million for the three months ended December 31, 2017. Digital engagement services revenue as a percentage of total revenue decreased to 45% from 52% for the three months ended December 31, 2018 compared to the prior period. The decrease as a percentage of total revenue is attributable to overall decreases in license revenues generating fewer service engagements.

Subscription and Perpetual Licenses

Revenue from subscription and perpetual licenses decreased $561 thousand, or 35%, to $1.0 million for the three months ended December 31, 2018 compared to $1.6 million for the three months ended December 31, 2017. The decrease for the three months ended December 31, 2018 compared to the prior period is primarily due to a decline in SaaS license revenue due to the loss of a large customer that we previously disclosed. Subscription and perpetual license revenue as a percentage of total revenue increased to 44% for the three months ended December 31, 2018 from 40% for the three months ended December 31, 2017.

Managed Service Hosting

Revenue from managed service hosting decreased $46 thousand, or 15%, to $257 thousand for the three months ended December 31, 2018 compared to $303 thousand for the three months ended December 31, 2017. The decrease is due to customer attrition offset by new hosting contracts entered into the current fiscal year. Managed services revenue as a percentage of total revenue increased to 11% for the three months ended December 31, 2018 from 8% for the three months ended December 31, 2017. The increase as a percentage of revenue is attributable to the overall decreases in other revenue streams.

Costs of Revenue

Total cost of revenue decreased $616 thousand to $1.3 million, or 31%, for the three months ended December 31, 2018 compared to $2.0 million for the three months ended December 31, 2017. The gross profit margin declined to 44% for the three months ended December 31, 2018 compared to 51% for the three months ended December 31, 2017. The decline in the gross profit margin for the three months ended December 31, 2018 compared to the three months ended December 31, 2017 is attributable to the decrease in digital engagement services revenue.

Cost of Digital Engagement Services

Cost of digital engagement services decreased $542 thousand, or 39%, to $855 thousand for the three months ended December 31, 2018 compared to $1.4 million for the three months ended December 31, 2017. The decrease is primarily due to a decrease in headcount. The cost of digital engagement services as a percentage of digital engagement services revenue increased to 80% for the three months ended December 31, 2018 from 68% compared to the three months ended December 31, 2017. The increase is due to an increase in third party subcontractor costs.

Cost of Subscription and Perpetual License

Cost of subscription and perpetual licenses decreased $57 thousand, or 12%, to $423 thousand for the three months ended December 31, 2018 compared to $480 thousand for the three months ended December 31, 2017. The cost of subscription and perpetual licenses as a percentage of subscription and perpetual license revenue increased to 40% for the three months ended December 31, 2018 from 30% compared to the three months ended December 31, 2017. The increase is attributable to fixed costs to operate our cloud-based hosting model with Amazon Web Services.

Cost of Managed Service Hosting

Cost of managed service hosting decreased $17 thousand, or 21%, to $63 thousand for the three months ended December 31, 2018 compared to $80 thousand for the three months ended December 31, 2017. The cost of managed services as a percentage of managed services revenue decreased to 25% for the three months ended December 31, 2018 from 26% compared to the three months ended December 31, 2017. While certain costs to operate our cloud-based model with Amazon Web Services are fixed, we were able to eliminate unnecessary variable costs.

Operating Expenses

Sales and Marketing Expenses

Sales and marketing expenses decreased $216 thousand to $814 thousand, or 21%, for the three months ended December 31, 2018 compared to $1.0 million for the three months ended December 31, 2017. Sales and marketing expenses represented 34% and 26% of total revenue for the three months ended December 31, 2018 and 2017, respectively. The decrease for the three months ended December 31, 2018 compared to the three months ended December 31, 2017 is attributable to decreases in headcount and the impact of new revenue recognition guidance, which allows companies to capitalize and then amortize sales commissions over the estimated customer life.

Support

Support expenses increased $17 thousand, or 23%, to $91 thousand for the three months ended December 31, 2018 compared to $74 thousand for the three months ended December 31, 2017. Support expenses represented 4% and 2% of total revenue for the three months ended December 31, 2018 and 2017, respectively. The increase in expense was due to increases in support headcount and personnel expenses.

General and Administrative Expenses

General and administrative expenses decreased $49 thousand, or 7%, to $687 thousand for the three months ended December 31, 2018 compared to $736 thousand for the three months ended December 31, 2017. General and administrative expenses represented 29% and 19% of total revenue for the three months ended December 31, 2018 and 2017, respectively. The decrease in expense was due to decreases in headcount and personnel expenses.

Research and Development

Research and development expense increased $11 thousand, or 3%, to $418 thousand for the three months ended December 31, 2018 compared to $407 thousand for the three months ended December 31, 2017. Research and development expenses represented 18% and 10% of total revenue for the three months ended December 31, 2018 and 2017, respectively. The increase in research and development expense is due to an increase in compensation expense.

Depreciation and Amortization

Depreciation and amortization expense decreased $82 thousand, or 76%, to $26 thousand for the three months ended December 31, 2018 compared to $108 thousand for the three months ended December 31, 2017. Depreciation and amortization has decreased due to asset retirements related to the termination and closing of offices, as well as reductions in capital expenditures. Depreciation and amortization represented 1% and 3% of total revenue for the three months ended December 31, 2018 and 2017, respectively.

Goodwill Impairment

The Company performed an interim impairment test, which resulted in an impairment charge of $3.7 million. An impairment charge is recognized for the amount by which the carrying amount exceeds the Company's fair value.

Net Loss

Loss from operations

The loss from operations was ($4.7) million for three months ended December 31, 2018, compared to a loss of ($343) thousand in the prior period. Operating expenses increased $3.4 million, or 145%, for the three months ended December 31, 2018 compared to December 31, 2017, which is primarily a goodwill impairment charge of $3.7 million. Excluding the goodwill impairment charge of $3.7 million, operating expenses decreased $319 thousand. We have made concerted efforts to bring our operating expenses in line with the decrease in expected revenues.

Income Taxes

The provision for income tax expense was $4 thousand and $1 thousand for the three months ended December 31, 2018 and 2017, respectively. Income tax expense represents the estimated liability for federal and state income taxes owed, including the alternative minimum tax. We have net operating loss carryforwards and other deferred tax benefits that are available to offset any potential taxable income.

Adjusted EBITDA

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

We believe this non-GAAP financial measure of Adjusted EBITDA is useful to management and investors in evaluating our operating performance for the periods presented and provide a tool for evaluating our ongoing operations.

Adjusted EBITDA, however, is not a measure of operating performance under GAAP and should not be considered as an alternative or substitute for GAAP profitability measures such as (i) income from operations and net income, or (ii) cash flows from operating, investing and financing activities, both as determined in accordance with GAAP. Adjusted

EBITDA as an operating performance measure has material limitations since it excludes the financial statement impact of income taxes, net interest expense, amortization of intangibles, depreciation, restructuring charges, goodwill impairment, other amortization and stock-based compensation, and therefore does not represent an accurate measure of profitability. As a result, Adjusted EBITDA should be evaluated in conjunction with net income for a complete analysis of our profitability, as net income includes the financial statement impact of these items and is the most directly comparable GAAP operating performance measure to Adjusted EBITDA. Our definition of Adjusted EBITDA may also differ from and therefore may not be comparable with similarly titled measures used by other companies, thereby limiting its usefulness as a comparative measure. Because of the limitations that Adjusted EBITDA has as an analytical tool, investors should not consider it in isolation, or as a substitute for analysis of our operating results as reported under GAAP.

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

	Three Months Ended December 31,	
	2018	**2017**
Net loss	$(4,955)	$(430)
Provision for income tax	4	1
Interest and other expense, net	217	86
Amortization of intangible assets	4	72
Depreciation	20	36
Goodwill impairment	3,732	-
Other amortization	15	16
Stock based compensation	97	125
Adjusted EBITDA	$(866)	$(94)

Adjusted EBITDA decreased compared to the first quarter of fiscal 2018. The decreases are primarily attributable to a decrease in revenues.

Liquidity and Capital Resources

Cash Flows

Operating Activities

Cash used in operating activities was $1.6 million for the three months ended December 31, 2018 compared to cash used in operating activities of $450 thousand for the three months ended December 31, 2017. This increase in the use of cash compared to the prior period was primarily due to an increase in accounts receivable and decrease in accounts payable.

Investing Activities

Cash used in investing activities was $18 thousand for the three months ended December 31, 2018 compared to $8 thousand for the three months ended December 31, 2017. Expenditures for property and equipment during the current fiscal year will not be material.

Financing Activities

Cash provided by financing activities was $3.0 million for the three months ended December 31, 2018 compared to $1.0 million for the three months ended December 31, 2017. Cash provided by financing activities for the three months ended December 31, 2018 is primarily attributable to the public offering in October 2018 (the “Offering”), whereby we sold an aggregate of (i) 1,424,000 Class A Units (the “*Class A Units*”) at a price of $0.50 per Class A Unit, consisting of (i) one share of the Company’s common stock and one five-year warrant to purchase one share of Company common stock at an exercise price of $0.50 and (ii) Preferred stock of 4,288 Class B Units, with each Class B Unit, convertible into 2,000 shares of the Company’s common stock at a conversion price of $0.50. Also, in October 2018, we repaid Promissory Term Notes in the amount of $954 thousand, which included interest of $13 thousand. The net proceeds to the Company from the Offering, after deducting the underwriter’s fees and expenses, the Company’s Offering expenses and the repayment of the Promissory Term Notes were approximately $3.4 million.

Capital Resources and Liquidity Outlook

We believe that the cash balance as of December 31, 2018 of $2.1 million as well as collections from accounts receivable will be sufficient to meet the Company’s obligations for a minimum of twelve months from the financial statement issuance date. Our borrowing facility with Heritage Bank of Commerce is subject to financial covenants that must be met. It is not certain that all or part of this line will be available to us in the future; and other sources of financing may not be available to us in a timely basis if at all, or on terms acceptable to us. If we fail to obtain acceptable funding when needed, we may not have sufficient resources to fund our normal operations, and this would have a material adverse effect on our business.

Off-Balance Sheet Arrangements

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

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

Commitments and Contingencies

As of December 31, 2018, we have no material commitments or contingencies.

Critical Accounting Policies

These critical accounting policies and estimates by our management were prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP") and should be read in conjunction with Note 2 *Summary of Significant Accounting Policies* to the Consolidated Financial Statements of our Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 28, 2018.

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

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

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

Revenue Recognition

The Company derives its revenue from three sources: (i) Software Licenses, which are comprised of subscription fees ("SaaS"), perpetual software licenses, and maintenance for post-customer support ("PCS") on perpetual licenses, (ii) Digital Engagement Services, which are professional services to implement our products such as web development, digital strategy, information architecture and usability engineering and (iii) hosting of perpetual licenses. Customers who license the software on a subscription basis, which can be described as "Software as a Service" or "SaaS" do not take possession of the software.

Revenue is recognized when control of these services is transferred to the Company's customers, in an amount that reflects the consideration the Company expects to be entitled to in exchange for those services. If the consideration promised in a contract includes a variable amount, for example, overage fees, contingent fees or service level penalties, the Company includes an estimate of the amount it expects to receive for the total transaction price if it is probable that a significant reversal of cumulative revenue recognized will not occur. The Company's subscription service arrangements are non-cancelable and do not contain refund-type provisions. Revenue is reported net of applicable sales and use tax.

The Company recognizes revenue from contracts with customers using a five-step model, which is described below:

- Identify the customer contract;
- Identify performance obligations that are distinct;
- Determine the transaction price;
- Allocate the transaction price to the distinct performance obligations; and
- Recognize revenue as the performance obligations are satisfied.

Allowance for Doubtful Accounts

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

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

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

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

Accounting for Goodwill and Intangible Assets

Goodwill is tested for impairment annually during the fourth quarter of every year and more frequently if events and circumstances indicate that the asset might be impaired. The purpose of an impairment test is to identify any potential impairment by comparing the carrying value of a reporting unit including goodwill to its fair value. An impairment charge is recognized for the amount by which the carrying amount exceeds the reporting unit’s fair value, however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit.

Factors that could lead to a future impairment include material uncertainties such as operational, economic and competitive factors specific to the key assumptions underlying the fair value estimate we use in our impairment testing that have reasonable possibility of changing. This could include a significant reduction in projected revenues, a deterioration of projected financial performance, future acquisitions and/or mergers, and a decline in our market value as a result of a significant decline in our stock price.

Accounting for Stock-Based Compensation

At December 31, 2018, we maintained two stock-based compensation plans, one of which has expired but still contains vested and unvested stock options and are more fully described in Note 12 to the Consolidated Financial Statements of our Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 28, 2018.

The Company accounts for stock-based compensation awards in accordance with ASC 718 *Compensation-Stock* Topic of the Codification. Share-based payments (to the extent they are compensatory) are recognized in our Consolidated Statements of Operations based on their fair values.

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

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

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

Item 3. Qualitative and Quantitative Disclosures About Market Risk.

Not required.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) were effective as of December 31, 2018.

Changes in Internal Control over Financial Reporting

There were no changes to our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) that occurred during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on Controls

Our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance of achieving the desired control objectives. Our management recognizes that any control system, no matter how well designed and operated, is based upon certain judgments and assumptions and cannot provide absolute assurance that its objectives will be met. Similarly, an evaluation of controls cannot provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

From time to time we are subject to ordinary routine litigation and claims incidental to our business. We are not currently involved in any legal proceedings that we believe are material beyond those previously disclosed in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 28, 2018.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

There were no sales of unregistered securities during the quarter ended December 31, 2018.

Item 6. Exhibits.

Exhibit No.	Description of Document
1.1	Underwriting Agreement (incorporated by reference to Exhibit 1.1 to our Form 8-K filed on October 19, 2018)
3.1	Amended and Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to our Quarterly Report on Form 10-Q filed on May 15, 2013)
3.2	Certificate of Amendment to Amended and Restated Certificate of Incorporation, dated May 4, 2015 (incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K filed on May 5, 2015)
3.3	Certificate of Designations of the Series A Convertible Preferred Stock (incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K filed on November 4, 2014)
3.4	Amended and Restated By-laws (incorporated by reference to Exhibit 3.1 to our current Report on Form 8-K filed on July 24, 2017)
3.5	Certificate of Designations of the Series B Convertible Preferred Stock (incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K filed on October 19, 2018)
3.6	Amended and Restated By-laws (incorporated by reference to Exhibit 3.1 to our current Report on Form 8-K filed on December 14, 2018)
4.1	Registration Rights Agreement, dated November 3, 2016, by and between Bridgeline Digital, Inc. and the Investors party thereto (incorporated by reference to Exhibit 10.3 to our Current Report on Form 8-K Filed on November 4, 2016)
4.2	Form of Warrant (incorporated by reference to Exhibit 1.1 to our Form 8-K filed on October 19, 2018)
10.1	Second Amendment to the Loan and Security Agreement between Bridgeline Digital, Inc and Montage Capital II, L.P. dated October 22, 2018 (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K Filed on October 24, 2018)
10.2	Tenth Amendment to the Loan and Security Agreement between Bridgeline Digital, Inc and Heritage Bank of Commerce, dated December 27, 2018 (incorporated by reference to Exhibit 10.46 to our Current Report on Form 10-K Filed on December 28, 2018)
10.3	Third Amendment to the Loan and Security Agreement between Bridgeline Digital, Inc and Montage Capital II, L.P. dated December 27, 2018 (incorporated by reference to Exhibit 10.47 to our Current Report on Form 10-K Filed on December 28, 2018)
10.4	Asset Purchase Agreement between Bridgeline Digital, Inc and Seevolution, Inc., Celebros Inc., and Elisha Gilboa, (collectively, the Sellers) dated February 13, 2019 (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K Filed on February 14, 2019)

10.5	Eleventh Amendment to the Loan and Security Agreement between Bridgeline Digital, Inc and Heritage Bank of Commerce, dated February 14, 2019
31.1	Certification required by Rule 13a-14(a) or Rule 15d-14(a).
31.2	Certification required by Rule 13a-14(a) or Rule 15d-14(a).
32.1	Certification required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350).

32.2	Certification required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350).
101.INS*	XBRL Instance
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation
101.DEF*	XBRL Taxonomy Extension Definition
101.LAB*	XBRL Taxonomy Extension Labels
101.PRE*	XBRL Taxonomy Extension Presentation

*Management compensatory plan

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

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.

	Bridgeline Digital, Inc. (Registrant)
February 14, 2019	/s/ Roger Kahn **Roger Kahn**
Date	**President and Chief Executive Officer** (Principal Executive Officer)
February 14, 2019	/s/ Carole Tyner **Carole Tyner**
Date	**Chief Financial Officer** (Principal Financial and Accounting Officer)