Form 10-Q

BLACKBOARD INC - BBBB

Filed: November 09, 2006 (period: September 30, 2006)

Table of Contents

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

FORM 10-Q

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

For the quarterly period ended September 30, 2006

OR

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

Commission file number 000-50784

Blackboard Inc.
(Exact Name of Registrant as Specified in Its Charter)

Delaware	**52-2081178**
(State or Other Jurisdiction of Incorporation or Organization)	*(I.R.S. Employer Identification No.)*
1899 L Street, N.W. **Washington D.C.**	**20036**
(Address of Principal Executive Offices)	*(Zip Code)*

Registrant's Telephone Number, Including Area Code:
(202) 463-4860

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer ☐ Accelerated filer ☑ Non-accelerated filer ☐

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

Class	Outstanding at October 31, 2006
Common Stock, $0.01 par value	28,068,526

Blackboard Inc.

Quarterly Report on Form 10-Q

For the Quarter Ended September 30, 2006
INDEX

Throughout this Quarterly Report on Form 10-Q, the terms "we," "us," "our" and "Blackboard" refer to Blackboard Inc. and its subsidiaries.

PART I — FINANCIAL INFORMATION

Consolidated Financial Statements

BLACKBOARD INC.
CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

	December 31, 2005	September 30, 2006 (Unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 75,895	$ 37,045
Short-term investments	62,602	—
Restricted cash	521	461
Accounts receivable, net of allowance for doubtful accounts of $701 and $733 at December 31, 2005 and September 30, 2006, respectively	26,136	61,360
Inventories	1,806	2,443
Prepaid expenses and other current assets	2,116	2,976
Deferred tax asset, current portion	10,274	16,818
Deferred cost of revenues, current portion	5,797	8,080
Total current assets	185,147	129,183
Deferred tax asset, non-current portion	12,023	12,386
Deferred cost of revenues, non-current portion	1,310	772
Deferred merger costs (WebCT, Inc.)	4,956	—
Property and equipment, net	9,940	13,276
Goodwill	10,252	102,725
Intangible assets, net	560	61,275
Total assets	$ 224,188	$ 319,617
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 1,833	$ 1,530
Accrued expenses	14,083	20,153
Term loan, current portion	—	600
Deferred rent, current portion	347	398
Deferred revenues, current portion	74,975	118,388
Total current liabilities	91,238	141,069
Term loan, noncurrent portion, net of debt discount of $1,539 at September 30, 2006	—	42,411
Deferred rent, noncurrent portion	426	233
Deferred revenues, noncurrent portion	2,199	3,290
Stockholders' equity:		
Preferred stock, $0.01 par value; 5,000,000 shares authorized, and no shares issued or outstanding at December 31, 2005 and September 30, 2006	—	—
Common stock, $0.01 par value; 200,000,000 shares authorized; 27,479,351 and 28,052,831 shares issued and outstanding at December 31, 2005 and September 30, 2006, respectively	275	280
Additional paid-in capital	210,805	224,027
Accumulated deficit	(80,755)	(91,693)
Total stockholders' equity	130,325	132,614
Total liabilities and stockholders' equity	$ 224,188	$ 319,617

See notes to unaudited consolidated financial statements.

BLACKBOARD INC.
UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share and per share data)

	Three Months Ended September 30, 2005	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2006
Revenues:				
Product	$ 31,301	$ 43,435	$ 88,341	$ 113,597
Professional services	4,626	6,919	11,577	18,046
Total revenues	35,927	50,354	99,918	131,643
Operating expenses:				
Cost of product revenues, excludes $2,800 and $6,533 in amortization of acquired technology included in amortization of intangibles resulting from acquisitions shown below for the three and nine months ended September 30, 2006, respectively(1)	7,507	11,354	21,818	29,348
Cost of professional services revenues(1)	2,733	4,385	7,499	12,061
Research and development(1)	3,657	8,000	10,162	20,157
Sales and marketing(1)	10,323	16,678	28,269	43,920
General and administrative(1)	5,032	9,661	14,464	27,063
Amortization of intangibles resulting from acquisitions	66	5,377	200	12,591
Total operating expenses	29,318	55,455	82,412	145,140
Income (loss) from operations	6,609	(5,101)	17,506	(13,497)
Other income (expense), net:				
Interest expense	(9)	(1,860)	(39)	(3,756)
Interest income	932	341	1,939	1,974
Other income (expense)	—	(155)	—	(301)
Income (loss) before (provision) benefit for income taxes	7,532	(6,775)	19,406	(15,580)
(Provision) benefit for income taxes	(263)	2,000	(664)	4,642
Net income (loss)	$ 7,269	$ (4,775)	$ 18,742	$ (10,938)
Net income (loss) per common share:				
Basic	$ 0.27	$ (0.17)	$ 0.71	$ (0.39)
Diluted	$ 0.25	$ (0.17)	$ 0.66	$ (0.39)
Weighted average number of common shares:				
Basic	26,986,242	27,922,879	26,529,922	27,760,438
Diluted	28,829,768	27,922,879	28,240,576	27,760,438
(1) Includes the following amounts related to stock-based compensation:				
Cost of product revenues	$ —	$ 113	$ —	$ 277
Cost of professional services revenues	—	150	—	519
Research and development	—	168	—	444
Sales and marketing	—	899	—	2,239
General and administrative	19	931	55	2,559

See notes to unaudited consolidated financial statements.

BLACKBOARD INC.
UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2006
	(In thousands)	
Cash flows from operating activities		
Net income (loss)	$ 18,742	$ (10,938)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Deferred income tax benefit	—	(6,078)
Excess tax benefits from stock-based compensation	—	(248)
Amortization of debt discount	—	940
Depreciation and amortization	5,003	6,572
Amortization of intangibles	200	12,591
Change in allowance for doubtful accounts	(24)	(143)
Noncash stock-based compensation	55	6,038
Changes in operating assets and liabilities:		
Accounts receivable	(11,490)	(30,712)
Inventories	(59)	(637)
Prepaid expenses and other current assets	(586)	496
Deferred cost of revenues	(1,959)	(1,745)
Accounts payable	111	(575)
Accrued expenses	797	(4,883)
Deferred rent	(221)	(142)
Deferred revenues	12,797	40,048
Net cash provided by operating activities	23,366	10,584
Cash flows from investing activities		
Acquisition of WebCT, Inc., net of cash acquired	—	(154,628)
Purchase of property and equipment	(6,696)	(8,188)
Purchase of held-to-maturity investments	(27,230)	—
Sale of held-to-maturity investments	5,750	23,546
Purchase of available-for-sale investments	(21,900)	—
Sale of available-for-sale investments	25,600	39,056
Net cash used in investing activities	(24,476)	(100,214)
Cash flows from financing activities		
Payments on equipment notes	(424)	—
Proceeds from revolving credit facility	—	10,000
Payments on revolving credit facility	—	(10,000)
Proceeds from term loan	—	57,522
Payments on term loan	—	(15,450)
Release of letter of credit	—	1,517
Excess tax benefits from stock-based compensation	—	248
Proceeds from exercise of stock options	8,222	6,943
Net cash provided by financing activities	7,798	50,780
Net increase (decrease) in cash and cash equivalents	6,688	(38,850)
Cash and cash equivalents at beginning of period	78,149	75,895
Cash and cash equivalents at end of period	$ 84,837	$ 37,045

See notes to unaudited consolidated financial statements.

BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
For the Nine Months Ended September 30, 2005 and 2006

In these Notes to Unaudited Consolidated Financial Statements, the terms "the Company" and "Blackboard" refer to Blackboard Inc. and its subsidiaries.

1. Nature of Business

Blackboard Inc. (the Company) is a leading provider of enterprise software applications and related services to the education industry. The Company's suites of products include the following products: *Blackboard Learning System™, Blackboard Community System™, Blackboard Content System™, Blackboard Transaction System™* and *Blackboard One™*.

On February 28, 2006, the Company completed its merger with WebCT, Inc. (WebCT) pursuant to the Agreement and Plan of Merger dated as of October 12, 2005.

2. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The results of operations for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the full fiscal year. The consolidated balance sheet at December 31, 2005 has been derived from the audited consolidated financial statements at that date but does not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements.

These consolidated financial statements should be read in conjunction with the audited consolidated financial statements as of December 31, 2004 and 2005 and for each of the three years in the period ended December 31, 2005 included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 15, 2006.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries after elimination of all significant intercompany balances and transactions. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

Foreign Currency Translation

The functional currency of the Company's foreign subsidiaries is the U.S. dollar. The Company remeasures the monetary assets and liabilities of its foreign subsidiaries, which are maintained in the local currency ledgers, at the rates of exchange in effect at month end. Revenues and expenses recorded in the local currency during the period are translated using average exchange rates for each month. Non-monetary assets and liabilities are translated using historical rates. Resulting adjustments from the remeasurement process are included in other income (expense) in the accompanying consolidated statements of operations.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Reclassification

Certain amounts in the prior periods' consolidated financial statements have been reclassified to conform to the current period presentation.

Fair Value of Financial Instruments

SFAS No. 107, *"Disclosures about Fair Value of Financial Instruments,"* requires disclosures of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate that value. Due to their short-term nature, the carrying amounts reported in the consolidated financial statements approximate the fair value for cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses. The fair value of the Company's long-term debt is based upon quoted market prices for the same and similar issuances giving consideration to quality, interest rates, maturity and other characteristics. As of September 30, 2006, the Company believes the carrying amount of its long-term debt approximates its fair value since the variable interest rate of the debt approximates a market rate.

Short-term Investments

All investments with original maturities of greater than 90 days are accounted for in accordance with Statement of Financial Accounting Standards (SFAS) No. 115, *"Accounting for Certain Investments in Debt and Equity Securities."* The Company determines the appropriate classification at the time of purchase. At September 30, 2006, the Company held no short-term investments.

Deferred Income Taxes

Deferred tax assets and liabilities are determined based on temporary differences between the financial reporting bases and the tax bases of assets and liabilities. Deferred tax assets are also recognized for tax net operating loss carryforwards. These deferred tax assets and liabilities are measured using the enacted tax rates and laws that will be in effect when such amounts are expected to reverse or be utilized. The realization of total deferred tax assets is contingent upon the generation of future taxable income. Valuation allowances are provided to reduce such deferred tax assets to amounts more likely than not to be ultimately realized.

Income tax provision includes U.S. federal, state and local income taxes and is based on pre-tax income or loss. The interim period provision or benefit for income taxes is based upon the Company's estimate of its annual effective income tax rate. In determining the estimated annual effective income tax rate, the Company analyzes various factors, including projections of the Company's annual earnings and taxing jurisdictions in which the earnings will be generated, the impact of state and local income taxes and the ability of the Company to use tax credits and net operating loss carryforwards.

Cost of Product Revenues

Cost of product revenues excludes amortization of acquired technology intangibles resulting from acquisitions, which is included as amortization of intangibles resulting from acquisitions. Amortization expense related to acquired technology for the three and nine months ended September 30, 2006 was $2.8 million and $6.5 million, respectively. There was no amortization expense related to acquired technology for the three and nine months ended September 30, 2005.

Basic and Diluted Net Income (Loss) per Common Share

Basic net income (loss) per common share excludes dilution for potential common stock issuances and is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. Stock options were not considered in the computation of diluted net (loss) per common share for the three and nine months ended September 30, 2006 as their effect is anti-dilutive.

The following schedule presents the calculation of basic and diluted net income (loss) per common share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2006	2005	2006
	(Unaudited) (In thousands, except share and per share amounts)			
Net income (loss)	$ 7,269	$ (4,775)	$ 18,742	$ (10,938)
Weighted average shares outstanding, basic	26,986,242	27,922,879	26,529,922	27,760,438
Dilutive effect of:				
Stock options related to the purchase of common stock	1,761,668	—	1,598,334	—
Warrants related to the purchase of common stock	81,858	—	112,320	—
Weighted average shares outstanding, diluted	28,829,768	27,922,879	28,240,576	27,760,438
Basic net income (loss) per common share	$ 0.27	$ (0.17)	$ 0.71	$ (0.39)
Diluted net income (loss) per common share	$ 0.25	$ (0.17)	$ 0.66	$ (0.39)

Stock-Based Compensation

Prior to January 1, 2006, the Company accounted for its stock-based compensation plans under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, *"Accounting for Stock Issued to Employees"* (APB No. 25), and related interpretations, as permitted by SFAS No. 123, *"Accounting for Stock-Based Compensation"* (SFAS 123). Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123 (revised 2005), *"Share-Based Payment"* (SFAS 123R), using the modified prospective transition method. Under the modified prospective transition method, compensation cost recognized in fiscal 2006 includes: (a) compensation cost for all equity-based payments granted prior to but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123 and (b) compensation cost for all equity-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated.

Comprehensive Net Income (Loss)

Comprehensive net income (loss) includes net income (loss), combined with unrealized gains and losses not included in earnings and reflected as a separate component of stockholders' equity. There were no material differences between net income (loss) and comprehensive net income (loss) for the three and nine months ended September 30, 2005 and 2006.

Recent Accounting Pronouncements

In July 2006, the FASB issued FASB Interpretation No. 48, *"Accounting for Uncertainty in Income taxes — an interpretation of FASB Statement No. 109"* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, *"Accounting for Income Taxes"* . It prescribes that a company should use a more-likely-than-not recognition threshold based on the technical merits of the tax position taken. Tax positions that meet the more-likely-than-not recognition threshold should be measured as the largest amount of the tax benefits, determined on a cumulative probability basis, which is more likely than not to be realized upon ultimate settlement in the financial statements. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of FIN 48 on its consolidated results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 157, *"Fair Value Measurements"* (SFAS 157). SFAS 157 provides enhanced guidance for using fair value to measure assets and liabilities. It clarifies the principle that fair value should be based on the assumptions market participants would use when pricing the asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS 157 on its consolidated results of operations and financial condition.

3. WebCT, Inc. Merger

On February 28, 2006, the Company completed its merger with WebCT pursuant to the Agreement and Plan of Merger dated as of October 12, 2005. Pursuant to the Agreement and Plan of Merger, the Company acquired all the outstanding common stock of WebCT in a cash transaction for approximately $178.3 million. The effective cash purchase price of WebCT before transaction costs was approximately $149.0 million, net of WebCT's February 28, 2006 cash balance of approximately $29.3 million. The Company has included the financial results of WebCT in its consolidated financial statements beginning February 28, 2006. The Company believes the acquisition of WebCT supports its long-term strategic direction. The Company believes its merger with WebCT will position it to meet the growing demands of academic institutions as the Company works together with academic institutions to redefine the way students and faculty interact.

The merger was accounted for under the purchase method of accounting in accordance with SFAS No. 141 (SFAS 141), *"Business Combinations."* Assets acquired and liabilities assumed were recorded at their fair values as of February 28, 2006. The total preliminary purchase price is $187.5 million, including the estimated acquisition related transaction costs of approximately $9.2 million. Acquisition related transaction costs include investment banking, legal and accounting fees, and other external costs directly related to the merger.

Preliminary Purchase Price Allocation

Under the purchase method of accounting, the total estimated purchase price as shown in the table below was allocated to WebCT's net tangible and intangible assets based on their estimated fair values as of February 28, 2006. The excess of the purchase price over the net tangible and identifiable intangible assets was recorded as goodwill. The preliminary allocation of the purchase price was based upon a preliminary valuation and the Company's estimates and assumptions are subject to change. The areas of the purchase price allocation that are not yet finalized relate primarily to income and non-income based taxes. In addition, upon the finalization of the combined company's legal entity structure, additional adjustments to deferred taxes may be required. Based on independent third party valuations, and other factors as described above, the preliminary estimated purchase price was allocated as follows (in thousands):

Cash and cash equivalents	$ 27,880
Restricted cash	1,452
Accounts receivable, net	4,369
Prepaid expenses and other current assets	1,356
Property and equipment, net	1,720
Deferred tax assets, net	486
Accounts payable	(272)
Other accrued liabilities	(10,856)
Deferred revenues	(4,456)
Net tangible assets to be acquired	21,679
Definite-lived intangible assets acquired	73,307
Goodwill	92,473
Total estimated purchase price	$ 187,459

Of the total estimated purchase price, a preliminary estimate of $21.7 million has been allocated to net tangible assets and $73.3 million has been allocated to definite-lived intangible assets acquired. Definite-lived intangible assets of $73.3 million consist of the value assigned to WebCT's customer relationships of $39.6 million and developed and core technology of $33.7 million.

The value assigned to WebCT's customer relationships was determined by discounting the estimated cash flows associated with the existing customers as of the acquisition date taking into consideration expected attrition of the existing customer base. The estimated cash flows were based on revenues for those existing customers net of operating expenses and net contributory asset charges associated with servicing those customers. The estimated revenues were based on revenue growth rates and customer renewal rates. Operating expenses were estimated based on the supporting infrastructure expected to sustain the assumed revenue growth rates. Net contributory asset charges were based on the estimated fair value of those assets that contribute to the generation of the estimated cash flows. A discount rate of 16% was deemed appropriate for valuing the existing customer base. The Company is amortizing the value of customer relationships proportionally to the respective discounted cash flows over an estimated useful life of five years. Customer relationships are not deductible for tax purposes.

Developed and core technology, which is comprised of products that have reached technological feasibility, includes products in WebCT's product line. The value assigned to WebCT's developed and core technology was determined by discounting the estimated future cash flows associated with the existing and core technologies to their present value. The revenue estimates used to value the developed and core technology were based on estimates of relevant market sizes and growth factors, expected trends in technology and the nature and expected timing of new product introductions by the Company and its competitors. The rates utilized to discount the net cash flows of developed and core technology to their present value were based on the risks associated with the respective cash flows taking into consideration the Company's weighted average cost of capital. A discount rate of 16% was deemed appropriate for valuing developed and core technology. The Company is amortizing the developed and core technology on a straight-line basis over an estimated useful life of three years. Developed and core technology are not deductible for tax purposes.

Of the total estimated purchase price, approximately $92.5 million has been allocated to goodwill. Goodwill represents the excess of the purchase price of an acquired business over the fair value of the net tangible and intangible assets acquired. Goodwill is not deductible for tax purposes.

BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

As a result of the WebCT acquisition, the Company recorded net deferred tax assets of approximately $486,000 in purchase accounting. This balance is comprised primarily of $36.0 million of deferred tax assets related to federal net operating losses, capitalized research and development, and certain amortization and depreciation expenses. The deferred tax assets are offset by $35.5 million in deferred tax liabilities resulting primarily from the related intangibles identified from the acquisition and the reduction in WebCT deferred revenues resulting from purchase accounting.

Deferred Revenues

In connection with the preliminary purchase price allocation, the estimated fair value of the support obligation assumed from WebCT in connection with the acquisition was determined utilizing a cost build-up approach. The cost build-up approach determines fair value by estimating the costs relating to fulfilling the obligation plus a normal profit margin. The sum of the costs and operating profit approximates, in theory, the amount that the Company would be required to pay a third party to assume the support obligation. The estimated costs to fulfill the support obligation were based on the historical direct costs related to providing the support services and to correct any errors in WebCT software products. These estimated costs did not include any costs associated with selling efforts or research and development or the related fulfillment margins on these costs. Profit associated with selling efforts is excluded because WebCT had concluded the selling effort on the support contracts prior to February 28, 2006. The estimated normal profit margin was determined to be 19%. As a result, in allocating the acquisition purchase price, the Company recorded an adjustment to reduce the carrying value of WebCT's February 28, 2006 deferred support revenue by approximately $14.3 million to $4.5 million which represents the Company's estimate of the fair value of the support obligation assumed. As former WebCT customers renew these support contracts, the Company will recognize revenue for the full value of the support contracts over the remaining term of the contracts, the majority of which are one year.

Pre-Acquisition Contingencies

The Company has currently not identified any material pre-acquisition contingencies where a liability is probable and the amount of the liability can be reasonably estimated. If information becomes available prior to the end of the purchase price allocation period, which would indicate that it is probable that such events had occurred and the amounts can be reasonably estimated, such items will be included in the purchase price allocation.

Pro Forma Financial Information

The unaudited financial information in the table below summarizes the combined results of operations of the Company and WebCT on a pro forma basis, as though the companies had been combined as of the beginning of each of the periods presented. The pro forma financial information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition and borrowings under the Company's senior secured credit facilities with Credit Suisse, Cayman Islands Branch (Credit Suisse) (see Note 7) had taken place at the beginning of each of the periods presented. The pro forma financial information for all periods presented also includes amortization expense from acquired intangible assets, adjustments to interest expense, interest income and related tax effects.

The unaudited pro forma financial information for the three and nine months ended September 30, 2006 combines the historical results for the Company for the three and nine months ended September 30, 2006 and the historical results for WebCT for the period from January 1, 2006 to February 28, 2006. The unaudited pro forma financial information for the three and nine months ended September 30, 2005 combines the historical results for the Company for the three and nine months ended September 30, 2005 and the historical results for WebCT for the same period.

BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2006	2005	2006
	(Unaudited) (In thousands, except per share amounts)			
Total revenues	$ 47,587	$ 50,354	$ 133,652	$ 139,648
Net income (loss)	$ 3	$ (4,775)	$ (812)	$ (15,137)
Basic net income (loss) per common share	$ 0.00	$ (0.17)	$ (0.03)	$ (0.55)
Diluted net income (loss) per common share	$ 0.00	$ (0.17)	$ (0.03)	$ (0.55)

4. Stock-Based Compensation

As a result of adopting SFAS 123R on January 1, 2006, the Company's loss before benefit for income taxes and net loss for the nine months ended September 30, 2006 were approximately $6.0 million and $4.2 million more, respectively, than if the Company had continued to account for stock-based compensation under APB No. 25. Basic and diluted net loss per common share for the nine months ended September 30, 2006 were each approximately $0.15 more than if the Company had not adopted SFAS 123R.

The following table illustrates the effect on net income (loss) and net income (loss) per common share if the Company had applied the fair value recognition provisions of SFAS 123R to stock-based compensation for the three and nine months ended September 30, 2005. The reported and pro forma net income (loss) and net income (loss) per common share for the three and nine months ended September 30, 2006 are the same because stock-based compensation is calculated under the provisions of SFAS 123R. The amounts for the three and nine months ended September 30, 2006 are included in the following table only to provide net income (loss) and net income (loss) per common share for a comparative presentation to the period of the previous year. The pro forma disclosure for the three and nine months ended September 30, 2005 utilized the Black-Scholes option-pricing formula to estimate the value of the respective options with such value amortized to expense over the options' vesting periods.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2006	2005	2006
	(Unaudited) (In thousands, except per share amounts)			
Pro forma net income (loss):				
As reported	$ 7,269	$ (4,775)	$ 18,742	$ (10,938)
Add: Stock-based compensation included in reported net income (loss)	19	—	55	—
Deduct: Stock-based compensation determined under fair value-based method for all awards	(1,623)	—	(4,260)	—
Pro forma net income (loss)	$ 5,665	$ (4,775)	$ 14,537	$ (10,938)
Net income (loss) per common share:				
Basic — as reported	$ 0.27	$ (0.17)	$ 0.71	$ (0.39)
Basic — pro forma	$ 0.21	$ (0.17)	$ 0.55	$ (0.39)
Diluted — as reported	$ 0.25	$ (0.17)	$ 0.66	$ (0.39)
Diluted — pro forma	$ 0.20	$ (0.17)	$ 0.51	$ (0.39)

The Company has utilized the Black-Scholes valuation model to estimate the fair value of the stock options granted during the nine months ended September 30, 2006, as well as for option grants during all prior periods. As follows are the weighted-average assumptions used in valuing the stock options granted during the nine months ended September 30, 2006, and a discussion of the Company's method.

BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Dividend yield	0%
Expected volatility	42.0%
Risk-free interest rate	4.8%
Expected life of options	4.93 years
Forfeiture rate	10%

Dividend yield — The Company has never declared or paid dividends on its common stock and does not anticipate paying dividends in the foreseeable future.

Expected volatility — Volatility is a measure of the amount by which a financial variable such as a share price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. Given the Company's limited historical stock data following its initial public offering in June 2004, the Company has used a blended volatility to best estimate expected volatility. The blended volatility includes the average of the Company's preceding one-year weekly historical volatility, the Company's preceding six-month market implied volatility and the Company's peer group preceding four-year weekly historical volatility. Market implied volatility is the volatility implied by the trading prices of publicly available stock options for the Company's common stock. The Company's peer group historical volatility includes the historical volatility of companies that are similar in revenue size, in the same industry or are competitors.

Risk-free interest rate — This is the average U.S. Treasury rate (having a term that most closely approximates the expected life of the option) for the period in which the option was granted.

Expected life of the options — This is the period of time that the options granted are expected to remain outstanding. This estimate is based primarily on historical exercise data. Options granted during the nine months ended September 30, 2006 have a maximum term of eight years.

Forfeiture rate — This is the estimated percentage of options granted that are expected to be forfeited or cancelled on an annual basis before becoming fully vested. The Company estimates the forfeiture rate based on past turnover data with further consideration given to the level of the employees to whom the options were granted.

The compensation cost that has been recognized in the Consolidated Statements of Operations for the Company's stock option plans for the nine months ended September 30, 2006 was approximately $6.0 million. The total income tax benefit recognized in the consolidated statements of operations for share-based compensation arrangements was approximately $217,000 for the nine months ended September 30, 2006. For stock subject to graded vesting, the Company has utilized the "straight-line" method for allocating compensation cost by period.

On June 14, 2006, at the Company's Annual Meeting of Stockholders, the Company's stockholders approved an amendment to the Company's Amended and Restated 2004 Stock Incentive Plan (the 2004 Plan) to increase the number of shares authorized for issuance under the 2004 Plan from 2,350,000 to 4,600,000.

As of September 30, 2006, approximately 2.2 million shares of common stock were available for future grants under the Company's 2004 Plan and no options were available for future grants under the Company's Amended and Restated Stock Incentive Plan adopted in 1998. Stock options granted under the 2004 Plan generally vest over a three-year period and have an eight-year expiration period. In October 2006, 147,500 options were granted under the 2004 Plan.

BLACKBOARD INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

A summary of option activity under the Company's option plans as of September 30, 2006, and changes during the nine months then ended are as follows (aggregate intrinsic value in thousands):

	Number of Shares	Weighted Average Price/Share	Aggregate Intrinsic Value
Options exercisable at December 31, 2005	1,903,411	$ 10.33	
Options outstanding at December 31, 2005	3,343,312	$ 13.06	
Granted	1,636,250	$ 27.60	
Exercised	(574,977)	$ 12.11	
Canceled	(389,389)	$ 24.16	
Options outstanding at September 30, 2006	4,015,196	$ 18.04	$ 35,908
Options exercisable at September 30, 2006	1,874,861	$ 11.33	$ 28,442

The weighted average remaining contractual life for all options outstanding under the Company's stock option plans at September 30, 2006 was 6.55 years. The weighted average remaining contractual life for exercisable stock options at September 30, 2006 was 5.64 years. The weighted average fair market value of the options at the date of grant for options granted during the nine months ended September 30, 2006 was $12.04. The total intrinsic value of stock options exercised during the nine months ended September 30, 2006 was approximately $8.7 million.

As of September 30, 2006, there was approximately $23.3 million of total unrecognized compensation cost related to unvested stock options granted under the Company's option plans. The cost is expected to be recognized through February 2013 with a weighted average recognition period of approximately 3.6 years.

5. Inventories

	December 31, 2005	September 30, 2006 (Unaudited)
	(In thousands)	
Raw materials	$ 700	$ 980
Work-in-process	451	594
Finished goods	655	869
Total inventories	$ 1,806	$ 2,443

6. Goodwill and Intangible Assets

The carrying amounts of goodwill and intangible assets as of December 31, 2005 and September 30, 2006 are as follows:

	December 31, 2005	September 30, 2006 (Unaudited)
	(In thousands)	
Goodwill	$ 10,252	$ 102,725
Acquired technology	$ 10,400	$ 44,107
Contracts and customer lists	5,443	45,042
Non-compete agreements	2,043	2,043
Trademarks and domain names	71	71
Subtotal	17,957	91,263
Less accumulated amortization	(17,397)	(29,988)
Intangible assets, net	$ 560	$ 61,275

Intangible assets from acquisitions are amortized over three to five years. Amortization expense related to intangible assets was approximately $200,000 and $12.6 million for the nine months ended September 30, 2005 and 2006, respectively. Amortization expense related to intangible assets for the years ended December 31, 2006, 2007, 2008, 2009, 2010 and 2011 is expected to be approximately $18.0 million, $21.5 million, $19.9 million, $8.5 million, $5.3 million and $845,000, respectively.

7. Debt

Credit Facilities

In connection with the acquisition of WebCT, the Company paid a portion of the purchase price using borrowings under a $70.0 million senior secured credit facilities agreement with Credit Suisse. The agreement provided for a $60.0 million senior secured term loan facility repayable over six years and a $10.0 million senior secured revolving credit facility due and payable in full at the end of five years. The interest rate on the facilities will accrue at one of the following rates selected by the Company: (a) adjusted LIBOR plus 2.25%-2.50% or (b) an alternate base rate plus 1.25%-1.50%. The alternate base rate is the higher of Credit Suisse's prime rate and the federal funds effective rate plus 0.5%. If the Company chooses the adjusted LIBOR interest rate option, interest payments are due on the last day of the interest period (one, two, three or six months) as selected by the Company. If the Company chooses the alternate base rate interest rate option, interest payments are due on the last day of each calendar quarter. During March 2006, the Company chose the alternate base rate interest rate option. As of March 31, 2006, the Company changed to the adjusted LIBOR interest rate option. At September 30, 2006 the interest rate on the term loan facility was 7.57%. This interest rate does not reflect the impact of the amortization of debt issuance costs, discussed below, as interest expense.

The Company repaid $10.0 million on the revolving credit facility on March 28, 2006. As of September 30, 2006, no amounts were outstanding on the revolving credit facility and $10.0 million in borrowings were available. The Company is required to pay a commitment fee, due at the end of each calendar quarter until the maturity date, equal to 0.5% on the average daily unused portion of the revolving credit facility as defined in the senior secured credit facilities agreement. The Company records this fee in interest expense.

A principal payment on the term loan facility in the amount of $150,000 is due on the last day of each quarter from March 31, 2006 through December 31, 2010 with a $14.3 million principal payment each due on March 31, 2011, June 30, 2011 and September 30, 2011. The remaining principal payment is due on February 28, 2012. The senior secured credit facilities agreement allows for voluntary principal prepayments of principal and requires mandatory principal prepayments within 90 days after calendar year-end based on a calculation of excess cash flow as defined in the senior secured credit facilities agreement. The Company repaid $10.0 million on the term loan facility on August 31, 2006 and $5.0 million on September 29, 2006. As of September 30, 2006, the Company had $44.6 million outstanding on the term loan facility. On October 31, 2006, the Company made a principal prepayment of $5.0 million.

In connection with obtaining the senior secured credit facilities, the Company incurred $2.5 million in debt issuance costs. These costs, which are recorded as a debt discount, are netted against the remaining principal amount outstanding. The debt discount will be amortized as interest expense using the effective interest method over the term of the senior secured credit facilities agreement and such amortization will be adjusted for any prepayments on the term loan facility. During the three months ended September 30, 2006, the Company recognized approximately $570,000 in additional interest expense associated with the acceleration in the amortization of the debt discount due to the prepayments of debt principal in August and September 2006 totaling $15.0 million. During the nine months ended September 30, 2006, the Company recorded amortization expense of approximately $1.0 million as interest expense.

Under the terms of the senior secured credit facilities agreement, the credit facilities are guaranteed by all of the Company's domestic subsidiaries and secured by perfected first priority security interests in, and mortgages on, substantially all of the Company's tangible and intangible assets (including the capital stock of each specified subsidiary) and each of the Company's subsidiaries. In addition, the facilities contain customary negative covenants applicable to the Company and its subsidiaries with respect to its operations and financial condition, such as a maximum quarterly capital expenditure amount ($16.0 million for the twelve months ended September 30, 2006), a maximum interest coverage ratio as defined in the senior secured credit facilities agreement of 4.00 to 1.00 and a minimum leverage ratio as defined in the senior secured credit facilities agreement of 3.25 to 1.00.

8. Commitments and Contingencies

The Company, from time to time, is subject to litigation relating to matters in the ordinary course of business. The Company believes that any ultimate liability resulting from these contingencies will not have a material adverse effect on the Company's results of operations, financial position or cash flows.

9. Quarterly Financial Information

The Company's quarterly operating results normally fluctuate as a result of seasonal variations in its business, principally due to the timing of client budget cycles and student attendance at client facilities. Historically, the Company has had lower new sales in its first and fourth quarters than in the remainder of the year. The Company's expenses, however, do not vary significantly with these changes and, as a result, such expenses do not fluctuate significantly on a quarterly basis. Historically, the Company has performed a disproportionate amount of its professional services, which are recognized as incurred, in its second and third quarters each year. The Company expects quarterly fluctuations in operating results to continue as a result of the uneven seasonal demand for its licenses and services offerings.

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

This report contains forward-looking statements. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words "believes," "anticipates," "plans," "expects," "intends" and similar expressions are intended to identify forward-looking statements. The important factors discussed under the caption "Risk Factors," presented below, could cause actual results to differ materially from those indicated by forward-looking statements made herein. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

General

We are a leading provider of enterprise software applications and related services to the education industry. Our clients use our software to integrate technology into the education experience and campus life, and to support activities such as a professor assigning digital materials on a class website; a student collaborating with peers or completing research online; an administrator managing a departmental website; or a merchant conducting cash-free transactions with students and faculty through pre-funded debit accounts. Our clients include colleges, universities, schools and other education providers, as well as textbook publishers and student-focused merchants who serve these education providers and their students.

We generate revenues from sales and licensing of products and from professional services. Our product revenues consist principally of revenues from annual software licenses, client hosting engagements and the sale of bundled software-hardware systems. We typically sell our licenses and hosting services under annually renewable agreements, and our clients generally pay the annual fees at the beginning of the contract term. We recognize revenues from these agreements, as well as revenues from bundled software-hardware systems, which do not recur, ratably over the contractual term, which is typically 12 months. Billings associated with licenses and hosting services are recorded initially as deferred revenues and then recognized ratably into revenues over the contract term. We also generate product revenues from the sale and licensing of third party software and hardware that is not bundled with our software. These revenues are generally recognized upon shipment of the products to our clients.

We derive professional services revenues primarily from training, implementation, installation and other consulting services. Substantially all of our professional services are performed on a time-and-materials basis. We recognize these revenues as the services are performed.

We typically license our individual applications either on a stand-alone basis or bundled as part of either of two suites, the *Blackboard Academic Suite™* and the *Blackboard Commerce Suite™.* The *Blackboard Academic Suite* includes the products formerly known as *WebCT Campus Edition™* and *WebCT Vista™*, which were acquired in our merger with WebCT, Inc.

The *Blackboard Academic Suite* includes:

- *Blackboard Learning System* basic products, which include:
  - *Blackboard Learning System — Basic License* and
  - *Blackboard Learning System — CE Basic License*,
- *Blackboard Learning System* enterprise products, which include:
  - *Blackboard Learning System — Enterprise License,*
  - *Blackboard Learning System — CE Enterprise License* and
  - *Blackboard Learning System — Vista Enterprise License*,
- *Blackboard Community System* and
- *Blackboard Content System*

The *Blackboard Commerce Suite* includes:

- *Blackboard Transaction System*,
- *Blackboard Community System* and
- *Blackboard One*

We generally price our software licenses on the basis of full-time equivalent students or users. Accordingly, annual license fees are generally greater for larger institutions.

Our operating expenses consist of cost of product revenues, cost of professional services revenues, research and development expenses, sales and marketing expenses, general and administrative expenses and amortization of intangibles resulting from acquisitions.

Major components of our cost of product revenues include license and other fees that we owe to third parties upon licensing software, and the cost of hardware that we bundle with our software. We initially defer these costs and recognize them into expense over the period in which the related revenue is recognized. Cost of product revenues also includes amortization of internally developed technology available for sale, employee compensation, stock-based compensation and benefits for personnel supporting our hosting, support and production functions, as well as related facility rent, communication costs, utilities, depreciation expense and cost of external professional services used in these functions. All of these costs are expensed as incurred. The costs of third-party software and hardware that is not bundled with software are also expensed when incurred, normally upon delivery to our client. Cost of product revenues excludes amortization of acquired technology intangibles resulting from acquisitions, which is included as amortization of intangibles resulting from acquisitions. Amortization expense related to acquired technology for the three and nine months ended September 30, 2006 was $2.8 million and $6.5 million, respectively. There was no amortization expense related to acquired technology for the three and nine months ended September 30, 2005.

Cost of professional services revenues primarily includes the costs of compensation, stock-based compensation and benefits for employees and external consultants who are involved in the performance of professional services engagements for our clients, as well as travel and related costs, facility rent, communication costs, utilities and depreciation expense used in these functions. All of these costs are expensed as incurred.

Research and development expenses include the costs of compensation, stock-based compensation and benefits for employees who are associated with the creation and testing of the products we offer, as well as the costs of external professional services, travel and related costs attributable to the creation and testing of our products, related facility rent, communication costs, utilities and depreciation expense. All of these costs are expensed as incurred.

Sales and marketing expenses include the costs of compensation, including bonuses and commissions, stock-based compensation and benefits for employees who are associated with the generation of revenues, as well as marketing expenses, costs of external marketing-related professional services, investor relations, facility rent, utilities, communications and travel attributable to those sales and marketing employees in the generation of revenues. All of these costs are expensed as incurred.

General and administrative expenses include the costs of compensation, stock-based compensation and benefits for employees in the human resources, legal, finance and accounting, management information systems, facilities management, executive management and other administrative functions that are not directly associated with the generation of revenues or the creation and testing of products. In addition, general and administrative expenses include the costs of external professional services and insurance, as well as related facility rent, communication costs, utilities and depreciation expense used in these functions.

Amortization of intangibles includes the amortization of costs associated with products, acquired technology, customer lists, non-compete agreements and other identifiable intangible assets. These intangible assets were recorded at the time of our acquisitions and relate to contractual agreements, technology and products that we continue to utilize in our business.

Critical Accounting Policies and Estimates

The discussion of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. During the preparation of these consolidated financial statements, we are required to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates and assumptions, including those related to revenue recognition, bad debts, fixed assets, long-lived assets, including purchase accounting and goodwill, and income taxes. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. The results of our analysis form the basis for making assumptions about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions, and the impact of such differences may be material to our consolidated financial statements. Our critical accounting policies have been discussed with the audit committee of our board of directors.

We believe that the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our consolidated financial statements:

Revenue recognition. Our revenues are derived from two sources: product sales and professional services sales. Product revenues include software license, hardware, premium support and maintenance, and hosting revenues. Professional services revenues include training and consulting services. We recognize software license and maintenance revenues in accordance with the American Institute of Certified Public Accountants' Statement of Position, or SOP, 97-2, *"Software Revenue Recognition,"* as modified by SOP 98-9, *"Modification of SOP 97-2, Software Revenue Recognition, with Respect to Certain Transactions."* Our software does not require significant modification and customization services. Where services are not essential to the functionality of the software, we begin to recognize software licensing revenues when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred; (3) the fee is fixed and determinable; and (4) collectibility is probable.

We do not have vendor-specific objective evidence, or VSOE, of fair value for our support and maintenance separate from our software. Accordingly, when licenses are sold in conjunction with our support and maintenance, we recognize the license revenue over the term of the maintenance service period.

We sell hardware in two types of transactions: sales of hardware in conjunction with our software licenses, which we refer to as bundled hardware-software systems, and sales of hardware without software, which generally involve the resale of third-party hardware. After any necessary installation services are performed, hardware revenues are recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred; (3) the fee is fixed and determinable; and (4) collectibility is probable. We have not determined VSOE of the fair value for the separate components of bundled hardware-software systems. Accordingly, when a bundled hardware-software system is sold, all revenue is recognized over the term of the maintenance service period. Hardware sales without software are recognized upon delivery of the hardware to our client.

Hosting revenues are recorded in accordance with Emerging Issues Task Force, or EITF, 00-3, *"Application of AICPA SOP 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware."* We recognize hosting fees and set-up fees ratably over the term of the hosting agreement.

We recognize professional services revenues, which are generally contracted on a time-and-materials basis and consist of training, implementation and installation services, as the services are provided.

We do not offer specified upgrades or incrementally significant discounts. Advance payments are recorded as deferred revenues until the product is shipped, services are delivered or obligations are met and the revenue can be recognized. Deferred revenues represent the excess of amounts invoiced over amounts recognized as revenues. We provide non-specified upgrades of our product only on a when-and-if-available basis.

Allowance for doubtful accounts. We maintain an allowance for doubtful accounts for estimated losses resulting from the inability, failure or refusal of our clients to make required payments. We analyze accounts receivable, 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, in our collection efforts. Although we believe that our reserves 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, which will result in increased expense in the period in which such determination is made.

Long-lived assets. We record our long-lived assets, such as property and equipment, at cost. We review the carrying value of our long-lived assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of assets may not be recoverable in accordance with the provisions of SFAS No. 144, *"Accounting for the Impairment or Disposal of Long-Lived Assets."* We evaluate these assets by examining estimated future cash flows to determine if their current recorded value is impaired. We evaluate these cash flows by using weighted probability techniques as well as comparisons of past performance against projections. Assets may also be evaluated by identifying independent market values. If we determine that an asset's carrying value is impaired, we will record a write-down of the carrying value of the identified asset and charge the impairment as an operating expense in the period in which the determination is made. Although we believe that the carrying values of our long-lived assets are appropriately stated, changes in strategy or market conditions or significant technological developments could significantly impact these judgments and require adjustments to recorded asset balances.

Purchase Accounting and Goodwill. As the result of acquisitions, any excess purchase price over the net tangible and identifiable intangible assets acquired are recorded as goodwill. A preliminary allocation of the purchase price to tangible and intangible net assets acquired is based upon a preliminary valuation and our estimates and assumptions may be subject to change. We assess the impairment of goodwill in accordance with SFAS No. 142, *"Goodwill and Other Intangible Assets."* Accordingly, we test our goodwill for impairment annually on October 1, or whenever events or changes in circumstances indicate an impairment may have occurred, by comparing its fair value to its carrying value. Impairment may result from, among other things, deterioration in the performance of the acquired business, adverse market conditions, adverse changes in applicable laws or regulations, including changes that restrict the activities of the acquired business, and a variety of other circumstances. If we determine that an impairment has occurred, we are required to record a write-down of the carrying value and charge the impairment as an operating expense in the period the determination is made. Although we believe goodwill is appropriately stated in our consolidated financial statements, changes in strategy or market conditions could significantly impact these judgments and require an adjustment to the recorded balance.

Deferred Income Taxes. Deferred tax assets and liabilities are determined based on temporary differences between the financial reporting bases and the tax bases of assets and liabilities. Deferred tax assets are also recognized for tax net operating loss carryforwards. These deferred tax assets and liabilities are measured using the enacted tax rates and laws that will be in effect when such amounts are expected to reverse or be utilized. The realization of total deferred tax assets is contingent upon the generation of future taxable income. Valuation allowances are provided to reduce such deferred tax assets to amounts more likely than not to be ultimately realized.

Income tax provision includes U.S. federal, state and local income taxes and is based on pre-tax income or loss. The interim period provision or benefit for income taxes is based upon our estimate of our annual effective income tax rate. In determining the estimated annual effective income tax rate, we analyze various factors, including projections of our annual earnings and taxing jurisdictions in which the earnings will be generated, the impact of state and local income taxes and our ability to use tax credits and net operating loss carryforwards.

Stock-Based Compensation. Prior to January 1, 2006, we accounted for our stock-based compensation plans under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, *"Accounting for Stock Issued to Employees"* (APB No. 25), and related interpretations, as permitted by SFAS No. 123, *"Accounting for Stock-Based Compensation"* (SFAS 123). Effective January 1, 2006, we adopted the fair value recognition provisions of SFAS No. 123 (revised 2005), *"Share-Based Payment"* (SFAS 123R), using the modified prospective transition method. Under the modified prospective transition method, compensation cost recognized in fiscal 2006 includes: (a) compensation cost for all equity-based payments granted prior to but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123 and (b) compensation cost for all equity-based payments granted subsequent to January 1, 2006 based on the grant date fair value estimated in accordance with the provisions of SFAS 123R.

As of September 30, 2006, there was approximately $23.3 million of total unrecognized compensation cost related to unvested stock options granted under our option plans. The cost is expected to be recognized through February 2013 with a weighted average recognition period of approximately 3.6 years.

Recent Accounting Pronouncements. In July 2006, the FASB issued FASB Interpretation No. 48, *"Accounting for Uncertainty in Income taxes — an interpretation of FASB Statement No. 109"* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, *"Accounting for Income Taxes"* . It prescribes that a company should use a more-likely-than-not recognition threshold based on the technical merits of the tax position taken. Tax positions that meet the more-likely-than-not recognition threshold should be measured as the largest amount of the tax benefits, determined on a cumulative probability basis, which is more likely than not to be realized upon ultimate settlement in the financial statements. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently evaluating the impact of FIN 48 on our consolidated results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 157, *"Fair Value Measurements"* (SFAS 157). SFAS 157 provides enhanced guidance for using fair value to measure assets and liabilities. It clarifies the principle that fair value should be based on the assumptions market participants would use when pricing the asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. SFAS 157 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of SFAS 157 on our consolidated results of operations and financial condition.

Important Factors Considered by Management

We consider several factors in evaluating both our financial position and our operating performance. These factors, while primarily focused on relevant financial information, also include other measures such as general market and economic conditions, competitor information and the status of the regulatory environment.

To understand our financial results, it is important to understand our business model and its impact on our consolidated financial statements. The accounting for the majority of our contracts requires us to initially record deferred revenues on our consolidated balance sheet upon invoicing the sale and then to recognize revenue in subsequent periods ratably over the term of the contract in our consolidated statements of operations. Therefore, to better understand our operations, one must look at both revenues and deferred revenues.

In evaluating our revenues, we analyze them in three categories: recurring ratable revenues, non-recurring ratable revenues and other revenues.

- Recurring ratable revenues include those product revenues that are recognized ratably over the contract term, which is typically one year, and that recur each year assuming clients renew their contracts. These revenues include revenues from the licensing of all of our software products, hosting arrangements and enhanced support and maintenance contracts related to our software products, including certain professional services performed by our professional services groups.

- Non-recurring ratable revenues include those product revenues that are recognized ratably over the term of the contract, which is typically one year, but that do not contractually recur. These revenues include certain hardware components of our *Blackboard Transaction System* products and certain third-party hardware and software sold to our clients in conjunction with our software licenses.

- Other revenues include those revenues that are recognized as earned and are not deferred to future periods. These revenues include professional services, the sales of *Blackboard One* , as well as the supplies and commissions we earn from publishers related to digital course supplement downloads.

In the case of both recurring ratable revenues and non-recurring ratable revenues, an increase or decrease in the revenues in one period would be attributable primarily to increases or decreases in sales in prior periods. Unlike recurring ratable revenues, which benefit both from new license sales and from the renewal of previously existing licenses, non-recurring ratable revenues primarily reflect one-time sales that do not contractually renew.

Other factors that we consider in making strategic cash flow and operating decisions include cash flows from operations, capital expenditures, total operating expenses and earnings.

Results of Operations

The following table sets forth selected unaudited consolidated statement of operations data expressed as a percentage of total revenues for each of the periods indicated.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2006	2005	2006
	(Unaudited)			
Revenues:				
Product	87 %	86 %	88 %	86 %
Professional services	13	14	12	14
Total revenues	100	100	100	100
Operating expenses:				
Cost of product revenues, excludes amortization of acquired technology included in amortization of intangibles resulting from acquisitions shown below	21	22	22	22
Cost of professional services revenues	8	9	8	9
Research and development	10	16	10	15
Sales and marketing	29	33	28	33
General and administrative	14	19	14	21
Amortization of intangibles resulting from acquisitions	0	11	0	10
Total operating expenses	82	110	82	110
Income (loss) from operations	18 %	(10)%	18 %	(10)%

Three Months Ended September 30, 2006 Compared to Three Months Ended September 30, 2005

Our total revenues for the three months ended September 30, 2006 were $50.4 million, representing an increase of $14.4 million, or 40.2%, as compared to $35.9 million for the three months ended September 30, 2005.

A detail of our total revenues by classification is as follows:

	Three Months Ended September 30,					
	2005			2006		
	Product	Services Revenues	Total	Product	Services Revenues	Total
	(Unaudited) (In millions)					
Recurring ratable revenues	$ 25.2	$ 0.2	$ 25.4	$ 34.7	$ 0.6	$ 35.3
Non-recurring ratable revenues	4.3	—	4.3	5.4	—	5.4
Other revenues	1.8	4.4	6.2	3.3	6.3	9.7
Total revenues	$ 31.3	$ 4.6	$ 35.9	$ 43.4	$ 6.9	$ 50.4

Product revenues. Product revenues, including domestic and international, for the three months ended September 30, 2006 were $43.4 million, representing an increase of $12.1 million, or 38.8%, as compared to $31.3 million for the three months ended September 30, 2005. Recurring ratable product revenues increased by $9.5 million, or 37.7%, for the three months ended September 30, 2006 as compared to the three months ended September 30, 2005. Product revenues from the *Blackboard Academic Suite* increased $7.6 million, or 45.7%, for the three months ended September 30, 2006 as compared to the three months ended September 30, 2005. This increase in *Blackboard Academic Suite* revenues was primarily due to a $6.4 million increase in revenues from *Blackboard Learning System* enterprise products, a $860,000 increase in revenues from *Blackboard Content System* licenses and a $340,000 increase in revenues from *Blackboard Community System* licenses. Product revenues from the *Blackboard Commerce Suite* increased by $390,000 due to an increase in revenues from *Blackboard Transaction System* licenses. The further increase in recurring ratable product revenues was due to a $1.2 million increase in hosting revenues and a $320,000 increase in revenues from enhanced support and maintenance revenues related to our software products. These increases in recurring ratable product revenues were attributable to current and prior period sales to new and existing clients, including clients resulting from the WebCT merger.

The increase in *Blackboard Learning System* enterprise products revenues was also attributable to the continued shift from the *Blackboard Learning System* basic products to the enterprise version of the *Blackboard Learning System.* The enterprise versions of the *Blackboard Learning System* products have additional functionality that is not available in the *Blackboard Learning System* basic products and consequently some *Blackboard Learning System* basic product clients upgrade to the enterprise versions of the *Blackboard Learning System.* Licenses of the enterprise versions of the *Blackboard Learning System* product have higher average pricing, which normally results in at least twice the contractual value as compared to *Blackboard Learning System* basic product licenses.

The increase in non-recurring ratable product revenues was primarily due to an increase in non-recurring third party hardware and software revenues.

The increase in other product revenues was primarily due to an increase in third party hardware and software revenues and an increase in publisher revenues due to the inclusion of WebCT publisher relationships.

Of our total revenues, our total international revenues for the three months ended September 30, 2006 were $9.3 million, representing an increase of $3.1 million, or 50.7%, as compared to $6.2 million for the three months ended September 30, 2005. International product revenues, which consist primarily of recurring ratable product revenues, were $8.2 million for the three months ended September 30, 2006, representing an increase of $2.6 million, or 46.3%, as compared to $5.6 million for the three months ended September 30, 2005. The increase in international recurring ratable product revenues was primarily due to an increase in international revenues from *Blackboard Academic Suite* products, which include former WebCT products, resulting from prior period sales to new and existing clients. The further increase in total international revenues was attributable to an increase in professional services revenues due to the increase in the number of international licensees of our *Blackboard Academic Suite* products, which generally purchase greater volumes of our service offerings. In addition, the increase in international revenues also reflects our investment in increasing the size of our international sales force and international marketing efforts during prior periods, which expanded our international presence and enabled us to sell more of our products to new and existing clients in our international markets.

Professional services revenues. Professional services revenues for the three months ended September 30, 2006 were $6.9 million, representing an increase of $2.3 million, or 49.6%, as compared to $4.6 million for the three months ended September 30, 2005. The increase in professional services was primarily attributable to an increase in the number and size of service engagements, which is directly related to the increase in the number of enterprise level licensees, which generally purchase greater volumes of our service offerings and increased sales of certain enhanced support and maintenance services. As a percentage of total revenues, professional services revenues for the three months ended September 30, 2006 were 13.7% as compared to 12.9% for the three months ended September 30, 2005. This increase was expected and was due primarily to the impact of purchase accounting adjustments to WebCT's beginning deferred revenue balances. As a result of the fair value adjustment to the acquired deferred revenue balances, we expect the percentage of professional services revenues to continue to remain higher than in prior years and for this trend to continue for the remainder of 2006.

Cost of product revenues. Our cost of product revenues for the three months ended September 30, 2006 was $11.4 million, representing an increase of $3.8 million, or 51.2%, as compared to $7.5 million for the three months ended September 30, 2005. The increase in cost of product revenues was primarily due to a $1.4 million increase in technical support costs primarily due to increased personnel costs related to increased headcount related to new hires during 2005 and 2006, higher average salaries due to annual salary increases in 2006 and the inclusion of WebCT's technical support groups. Further, the increase in cost of product revenues was due to a $1.3 million increase in expenses for our hosting services due to the increase in the number of clients, including WebCT clients, contracting for our hosting services, a $650,000 increase in third party hardware and software costs primarily associated with third party products sold with the *Blackboard Transaction System* and a $325,000 increase in commissions owed to publishers related to digital course supplement downloads. Cost of product revenues as a percentage of product revenues increased to 26.1% for the three months ended September 30, 2006 from 24.0% for the three months ended September 30, 2005. This decrease in product revenues margin was due primarily to the fair value adjustment to the acquired WebCT deferred revenue balances. Consequently, we expect our product revenues margins to continue to remain lower than in prior years and we expect this trend to continue for the remainder of 2006.

Cost of product revenues excludes amortization of acquired technology intangibles resulting from acquisitions, which is included as amortization of intangibles resulting from acquisitions. Amortization expense related to acquired technology for the three months ended September 30, 2006 was $2.8 million. There was no amortization expense related to acquired technology for the three months ended September 30, 2005. Cost of product revenues, including amortization of acquired technology, as a percentage of product revenues was 32.6% for the three months ended September 30, 2006 as compared to 24.0% for the three months ended September 30, 2005.

Cost of professional services revenues. Our cost of professional services revenues for the three months ended September 30, 2006 was $4.4 million, representing an increase of $1.7 million, or 60.4%, from $2.7 million for the three months ended September 30, 2005. The increase was directly related to the increase in professional services revenues. Further, for the three months ended September 30, 2006 there was approximately $150,000 in stock-based compensation included in cost of professional services revenues. Cost of professional services revenues as a percentage of professional services revenues increased to 63.4% for the three months ended September 30, 2006 from 59.1% for the three months ended September 30, 2005. The decrease in professional services revenues margin was primarily due to an increase in personnel costs due to an increase in staffing necessary to manage the increase in the number and size of service engagements throughout the year.

Research and development expenses. Our research and development expenses for the three months ended September 30, 2006 were $8.0 million, representing an increase of $4.3 million, or 118.8%, as compared to $3.7 million for the three months ended September 30, 2005. This increase was primarily attributable to an increase of approximately $3.6 million in personnel costs due to increased headcount related to new hires during 2005 and 2006, higher average salaries due to annual salary increases in 2006 and the inclusion of WebCT's research and development groups, including approximately $700,000 in severance costs related to the elimination of redundant positions. In addition, there was a $400,000 increase in professional service expenses resulting from our continued efforts to increase the functionality of our products. Further, for the three months ended September 30, 2006 there was approximately $170,000 in stock-based compensation included in research and development expenses.

Sales and marketing expenses. Our sales and marketing expenses for the three months ended September 30, 2006 were $16.7 million, representing an increase of $6.4 million, or 61.6%, as compared to $10.3 million for the three months ended September 30, 2005. This increase was primarily attributable to a $4.3 million increase in personnel costs due to increased headcount related to new hires during 2005 and 2006, higher average salaries due to annual salary increases in 2006 and the inclusion of WebCT's sales and marketing groups. In addition, there was a $1.0 million increase in general marketing activities primarily associated with WebCT's Users Conference in July 2006. In addition, there was a $200,000 change in bad debt expense for the three months ended September 30, 2006 as compared to the three months ended September 30, 2005 due to a $200,000 reduction in bad debt expense during the three months ended September 30, 2005. We did not record any bad debt expense during the three months ended September 30, 2006. Further, for the three months ended September 30, 2006 there was approximately $900,000 in stock-based compensation included in sales and marketing expenses.

General and administrative expenses. Our general and administrative expenses for the three months ended September 30, 2006 were $9.7 million, representing an increase of $4.6 million, or 92.0%, as compared to $5.0 million for the three months ended September 30, 2005. This increase was primarily attributable to an $1.5 million increase in personnel costs due to increased headcount related to new hires during 2005 and 2006, higher average salaries across all general and administrative functional departments due to annual salary increases in 2006 and the inclusion of WebCT's general and administrative functional departments. Further, there was a $500,000 increase in facility expenses, including rent, utilities, repairs and maintenance expenses, related to an increase in office space at our Washington, D.C. headquarters and international locations during 2005 and 2006, as well as the inclusion of WebCT office space in Lynnfield, MA and Canada. There was an $850,000 increase in professional service expenses during the three months ended September 30, 2006 as compared to the three months ended September 30, 2005 primarily associated with increased legal, accounting and integration costs resulting from the acquisition of WebCT. For the three months ended September 30, 2006, there was approximately $930,000 in stock-based compensation included in general and administrative expenses and we recorded approximately $600,000 in severance costs primarily for WebCT employees.

Net interest income (expense). Our net interest expense for the three months ended September 30, 2006 was $1.5 million as compared to net interest income of $923,000 for the three months ended September 30, 2005. This decrease was attributable primarily to interest expense associated with the credit facilities agreement we entered into with Credit Suisse, Cayman Islands Branch (Credit Suisse) to fund a portion of the acquisition of WebCT. In addition, we recognized approximately $570,000 in additional interest expense associated with the acceleration in the amortization of debt issuance costs due to the prepayments of debt principal in August and September 2006 totaling $15.0 million. Further, the net interest expense for the three months ended September 30, 2006 was due in part to lower cash and cash equivalent and short-term investment balances during the three months ended September 30, 2006 as compared to the three months ended September 30, 2005 resulting from the use of cash for the acquisition of WebCT.

Other income (expense). Our other expense for the three months ended September 30, 2006 was $155,000 and pertains to the remeasurement of our foreign subsidiaries ledgers, which are maintained in the local foreign currency, into the United States Dollar. In particular, this expense is primarily the result of the negative impact of the month-end change in the Canadian Dollar exchange rate to the United States Dollar from June to September on intercompany debt with our Canadian subsidiary.

Income taxes. Our benefit for income taxes for the three months ended September 30, 2006 was $2.0 million as compared to a provision for income taxes of $263,000 for the three months ended September 30, 2005. The benefit for income taxes for the three months ended September 30, 2006 was due to our loss for the period.

Net income (loss). As a result of the foregoing, we reported a net loss of $4.8 million for the three months ended September 30, 2006 as compared to net income of $7.3 million for the three months ended September 30, 2005.

Nine Months Ended September 30, 2006 Compared to Nine Months Ended September 30, 2005

Revenues. Our total revenues for the nine months ended September 30, 2006 were $131.6 million, representing an increase of $31.7 million, or 31.8%, as compared to $99.9 million for the nine months ended September 30, 2005.

A detail of our total revenues by classification is as follows:

	Nine Months Ended September 30,					
	2005			2006		
	Product	Services Revenues	Total	Product Revenues	Services Revenues	Total
	(Unaudited) (In millions)					
Recurring ratable revenues	$ 70.0	$ 0.6	$ 70.6	$ 91.5	$ 1.4	$ 92.9
Non-recurring ratable revenues	13.6	—	13.6	14.6	—	14.6
Other revenues	4.7	11.0	15.7	7.5	16.6	24.1
Total revenues	$ 88.3	$ 11.6	$ 99.9	$ 113.6	$ 18.0	$ 131.6

Product revenues. Product revenues, including domestic and international, for the nine months ended September 30, 2006 were $113.6 million, representing an increase of $25.3 million, or 28.6%, as compared to $88.3 million for the nine months ended September 30, 2005. Recurring ratable product revenues increased by $21.3 million, or 30.5%, for the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005. Product revenues from the *Blackboard Academic Suite* increased $16.6 million, or 36.2%, for the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005. This increase in *Blackboard Academic Suite* revenues was primarily due to a $12.6 million increase in revenues from *Blackboard Learning System* enterprise products, a $2.4 million increase in revenue from *Blackboard Content System* licenses and a $1.5 million increase in revenue from *Blackboard Community System* licenses. Product revenues from the *Blackboard Commerce Suite* increased by $1.1 million due to an increase in revenues from *Blackboard Transaction System* licenses. The further increase in recurring ratable product revenues was due to a $2.8 million increase in hosting revenues and a $770,000 increase in revenues from enhanced support and maintenance revenues related to our software products. These increases in recurring ratable product revenues were attributable to current and prior period sales to new and existing clients, including clients resulting from the WebCT merger.

The increase in *Blackboard Learning System* enterprise product revenue was also attributable to the continued shift from the *Blackboard Learning System* basic products to the enterprise versions of the *Blackboard Learning System.* The enterprise versions of the *Blackboard Learning System* products have additional functionality that is not available in the *Blackboard Learning System* basic products and consequently some *Blackboard Learning System* basic product clients upgrade to the *Blackboard Learning System* enterprise products. Licenses of the enterprise version of the *Blackboard Learning System* enterprise products have higher average pricing, which normally results in at least twice the contractual value as compared to *Blackboard Learning System* basic product licenses.

The increase in non-recurring ratable product revenues was primarily due to an increase in non-recurring third party hardware and software revenues.

The increase in other product revenues was primarily due to a $1.4 million increase in publisher revenues attributable to WebCT publisher relationships, a $600,000 increase in non-ratable, non-recurring third party hardware and software revenues, a $470,000 increase in non-ratable, non-recurring hosting revenues and a $385,000 increase in *Blackboard One* revenues due to an increase in current period sales.

Of our total revenues, our total international revenues for the nine months ended September 30, 2006 were $24.2 million, representing an increase of $7.1 million, or 41.1%, as compared to $17.1 million for the nine months ended September 30, 2005. International product revenues, which consist primarily of recurring ratable product revenues, were $21.1 million, representing an increase of $5.4 million, or 34.8%, as compared to $15.6 million for the nine months ended September 30, 2005. The increase in international revenues was driven primarily by an increase in recurring ratable product revenues. This increase was primarily due to an increase in international revenues from *Blackboard Academic Suite* products, which include former WebCT products, resulting from prior period sales to new and existing clients. The increase in international *Blackboard Academic Suite* revenues was primarily attributable to the same factors that contributed to the increase in overall *Blackboard Academic Suite* revenues. The further increase in total international revenues was attributable to an increase in professional services revenues due to the increase in the number of international licensees of our *Blackboard Academic Suite* products, which generally purchase greater volumes of our service offerings. In addition, the increase in international revenues also reflects our investment in increasing the size of our international sales force and international marketing efforts during prior periods, which expanded our international presence and enabled us to sell more of our products to new and existing clients in our international markets.

Professional services revenues. Professional services revenues for the nine months ended September 30, 2006, were $18.0 million, representing an increase of $6.5 million, or 55.9%, as compared to $11.6 million for the nine months ended September 30, 2005. The increase in professional services revenues was primarily attributable to an increase in the number and size of service engagements, which was directly related to the increase in the number of enterprise level licensees, which generally purchase greater volumes of our service offerings and increased sales of certain enhanced support and maintenance services. As a percentage of total revenues, professional services revenues for the nine months ended September 30, 2006 were 13.7%, as compared to 11.6% for the nine months ended September 30, 2005. As a result of the fair value adjustment to the acquired WebCT deferred revenue balances, we expect the percentage of professional services revenues to continue to remain higher than in prior years and for this trend to continue for the remainder of 2006.

Cost of product revenues. Our cost of product revenues for the nine months ended September 30, 2006 was $29.3 million, representing an increase of $7.5 million, or 34.5%, as compared to $21.8 million for the nine months ended September 30, 2005. The increase in cost of product revenue was primarily due to a $3.4 million increase in our technical support expense primarily due to increased personnel costs related to increased headcount related to new hires during 2005 and 2006, higher average salaries due to annual salary increases in 2006 and the inclusion of WebCT's technical support groups. In addition, there was a $2.9 million increase in expenses for our hosting services due to the increase in the number of clients, including WebCT clients, contracting for our hosting services. Further, the increase was due to a $700,000 increase in commissions owed to publishers related to digital course supplement downloads and a $400,000 increase in third party hardware and software costs primarily associated with third party products sold with the *Blackboard Transaction System.* Cost of product revenues as a percentage of product revenues increased to 25.8% for the nine months ended September 30, 2006 from 24.7% for the nine months ended September 30, 2005. This decrease in product revenues margin was due primarily to the fair value adjustment to the acquired WebCT deferred revenue balances. Consequently, we expect our product revenues margins to continue to remain lower than in prior years and we expect this trend to continue for the remainder of 2006.

Cost of product revenues excludes amortization of acquired technology intangibles resulting from acquisitions, which is included as amortization of intangibles resulting from acquisitions. Amortization expense related to acquired technology for the nine months ended September 30, 2006 was $6.6 million. There was no amortization expense related to acquired technology for the nine months ended September 30, 2005. Cost of product revenues, including amortization of acquired technology, as a percentage of product revenues was 31.6% for the nine months ended September 30, 2006 as compared to 24.7% for the nine months ended September 30, 2005.

Cost of professional services revenues. Our cost of professional services revenues for the nine months ended September 30, 2006 was $12.1 million, representing an increase of $4.6 million, or 60.8%, from $7.5 million for the nine months ended September 30, 2005. The increase in cost of professional services revenues was directly related to the increase in professional services revenues. Cost of professional services revenues as a percentage of professional services revenues increased to 66.8% for the nine months ended September 30, 2006 from 64.8% for the nine months ended September 30, 2005. The decrease in professional services revenues margin was primarily due to approximately $520,000 in stock-based compensation included in cost of professional services revenues for the nine months ended September 30, 2006.

Research and development expenses. Our research and development expenses for the nine months ended September 30, 2006 were $20.2 million, representing an increase of $10.0 million, or 98.4%, as compared to $10.2 million for the nine months ended September 30, 2005. This increase was primarily attributable to an $8.0 million increase in personnel-related costs due to increased headcount related to new hires during 2005 and 2006, higher average salaries due to annual salary increases in 2006 and the inclusion of WebCT's research and development groups, including approximately $700,000 in severance costs related to the elimination of redundant positions. In addition, there was a $1.1 million increase in professional services costs resulting from our continued efforts to increase the functionality of our products and a $200,000 increase in software and equipment expenses to support research and development activities. Further, for the nine months ended September 30, 2006 there was approximately $440,000 in stock-based compensation included in research and development expenses.

Sales and marketing expenses. Our sales and marketing expenses for the nine months ended September 30, 2006 were $43.9 million, representing an increase of $15.7 million or 55.4%, as compared to sales and marketing expense of $28.3 million for the nine months ended September 30, 2005. This increase was primarily attributable to a $10.2 million increase in personnel costs primarily due to increased headcount related to new hires during 2005 and 2006, higher average salaries due to annual salary increases in 2006 and the inclusion of WebCT's sales and marketing groups. Further, there was a $1.2 million change in bad debt expense for the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005 due to a $1.2 million reduction in bad debt expense during the nine months ended September 30, 2005. We did not record any bad debt expense during the nine months ended September 30, 2006. In addition, there was a $2.0 million increase in general marketing activities primarily associated with a larger annual Users Conference in February 2006 and the WebCT Users Conference in July 2006. Further, there was approximately $2.2 million in stock-based compensation included in sales and marketing expenses for the nine months ended September 30, 2006.

General and administrative expenses. Our general and administrative expenses for the nine months ended September 30, 2006 were $27.1 million, representing an increase of $12.6 million, or 87.1%, as compared to general and administrative expenses of $14.5 million for the nine months ended September 30, 2005. This increase was primarily attributable to a $4.2 million increase in personnel costs due to increased headcount related to new hires during 2005 and 2006, higher average salaries across all general and administrative functional departments due to annual salary increases in 2006 and the inclusion of WebCT general and administrative functional departments. Further, there was a $2.0 million increase in facility expenses, including rent, utilities, repairs and maintenance expenses, related to an increase in office space at our Washington, D.C. headquarters and international locations during 2005 and 2006, as well as the inclusion of WebCT office space in Lynnfield, MA and Canada. There was a $1.5 million increase in professional services expenses during the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005 primarily associated with increased legal, accounting and acquisition costs resulting from the acquisition of WebCT. For the nine months ended September 30, 2006, there was approximately $2.6 million in stock-based compensation included in general and administrative expenses and we recorded approximately $2.1 million in retention bonuses and severance costs primarily for WebCT employees.

Net interest income (expense). Our net interest expense for the nine months ended September 30, 2006 was $1.8 million as compared to net interest income of $1.9 million for the nine months ended September 30, 2005. This change was attributable primarily to our interest expense associated with the credit facilities agreement we entered into with Credit Suisse to fund a portion of the acquisition of WebCT. In addition, we recognized approximately $570,000 in additional interest expense associated with the acceleration in the amortization of debt issuance costs due to the prepayments of debt principal in August and September 2006 totaling $15.0 million. Further, this change was due in part to lower cash and cash equivalent and short-term investment balances during the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005 resulting from the use of cash for the acquisition of WebCT.

Other expense. Our other expense for the nine months ended September 30, 2006 was $301,000 and pertains to the remeasurement of our foreign subsidiaries ledgers, which are maintained in the local foreign currency, into the United States Dollar. In particular, this expense was primarily the result of the negative impact of the month-end change in the Canadian Dollar exchange rate to the United States Dollar from February to September on intercompany debt with our Canadian subsidiary.

Income taxes. Our benefit for income taxes for the nine months ended September 30, 2006 was $4.6 million as compared to a provision for income taxes of $664,000 for the nine months ended September 30, 2005. The benefit for income taxes for the nine months ended September 30, 2006 was due to our loss for the period.

Net income (loss). As a result of the foregoing, we reported a net loss of $10.9 million for the nine months ended September 30, 2006 as compared to net income of $18.7 million for the nine months ended September 30, 2005.

Liquidity and Capital Resources

We recognize revenues on annually renewable agreements, which results in deferred revenues. Deferred revenues as of September 30, 2006 were $121.7 million, representing an increase of $44.5 million, or 57.7%, from $77.2 million as of December 31, 2005. This increase was expected due to the seasonal variations in our business. We historically have lower sales to new and existing clients in our fourth quarter due to the timing of our clients' budget cycles and the renewal dates for our existing clients' annual licenses. Deferred revenues increased due to the higher volume of new sales to new and existing clients and the higher level of renewing licenses during the nine months ended September 30, 2006 as compared to the fourth quarter of 2005, offset by the recognition of revenues from prior period sales.

Our cash and cash equivalents were $37.0 million at September 30, 2006 compared to $75.9 million at December 31, 2005. The decrease in cash and cash equivalents was primarily due to the use of cash for the acquisition of WebCT.

Net cash provided by operating activities was $10.6 million during the nine months ended September 30, 2006 as compared to $23.4 million during the nine months ended September 30, 2005. This change for the nine months ended September 30, 2006 compared to the nine months ended September 30, 2005 was primarily due to a net loss of $10.9 million for the nine months ended September 30, 2006 as compared to net income of $18.7 million for the nine months ended September 30, 2005 which was primarily a result of the acquisition of WebCT; decreased accrued expenses, net of accrued expenses assumed in the acquisition of WebCT of approximately $10.9 million, which was primarily due to payment of accrued bonuses and commissions related to 2005 during the nine months ended September 30, 2006; and increased accounts receivable due to an increase in invoicing associated with increased sales to new and existing clients during 2006 as compared to 2005. These decreases were offset, in part, by an increase in deferred revenues primarily associated with the increase in invoicing associated with increased sales to new and existing clients during 2006 as compared to 2005 and an increase in amortization of intangibles resulting from our acquisition of WebCT.

Net cash used in investing activities was $100.2 million during the nine months ended September 30, 2006, an increase of $75.7 million, or 309.4%, from $24.5 million during the nine months ended September 30, 2005. This increase in cash usage was primarily due to the $154.6 million in net cash paid related to the acquisition of WebCT. This increase was offset by the sale of $62.6 million in short-term investments to fund a portion of the acquisition of WebCT. Cash expenditures for purchase of property and equipment were $8.2 million for the nine months ended September 30, 2006, which represents approximately 6.2% of total revenues for the nine months ended September 30, 2006. We expect cash expenditures for purchases of property and equipment to remain in the range 6% to 7% of total revenues in future periods.

Net cash provided by financing activities was $50.8 million during the nine months ended September 30, 2006 as compared to net cash provided by financing activities of $7.8 million during the nine months ended September 30, 2005. This change was primarily due to the $67.5 million in proceeds, net of $2.5 million in debt issuance costs, associated with the credit facilities agreement we entered into with Credit Suisse to fund a portion of the acquisition of WebCT. In March 2006, we repaid the $10.0 million revolving credit facility. In August and September 2006, we repaid $10.0 million and $5.0 million, respectively, on the term loan facility and made our recurring principal payments of $150,000 on the last day of each of the first three quarters. During the nine months ended September 30, 2006, we also received $6.9 million in proceeds from exercise of stock options as compared to $8.2 million for the nine months ended September 30, 2005.

In connection with the acquisition of WebCT, we paid a portion of the purchase price pursuant to a $70.0 million senior secured credit facilities agreement with Credit Suisse. The agreement provided for a $60.0 million senior secured term loan facility repayable over six years and a $10.0 million senior secured revolving credit facility due and payable in full at the end of five years. The interest on the facilities accrues at one of the following rates selected by us: (a) adjusted LIBOR plus 2.25%-2.50% or (b) an alternate base rate plus 1.25%-1.50%. The alternate base rate is the higher of Credit Suisse's prime rate and the federal funds effective rate plus 0.5%. If we choose the adjusted LIBOR interest rate option, interest payments are due on the last day of the interest period (one, two, three or six months) as selected by us. If we choose the alternate base rate interest rate option, interest payments are due on the last day of each calendar quarter. During March 2006, we chose the alternate base rate interest rate option. As of March 31, 2006, we changed to the adjusted LIBOR interest rate option. At September 30, 2006, the interest rate on the term loan facility was 7.57%. This interest rate does not reflect the impact of the amortization of debt issuance costs, discussed below, as interest expense.

We repaid $10.0 million on the revolving credit facility on March 28, 2006. As of March 31, 2006, no amounts were outstanding on the revolving credit facility and $10.0 million in borrowings were available. We are required to pay a commitment fee, due at the end of each calendar quarter until the maturity date, equal to 0.5% on the average daily unused portion of the revolving credit facility as defined in the senior secured credit facilities agreement. We record this fee in interest expense.

A principal payment on the term loan facility in the amount of $150,000 is due on the last day of each quarter from March 31, 2006 through December 31, 2010 with a $14.3 million principal payment each due on March 31, 2011, June 30, 2011 and September 30, 2011. The remaining principal payment is due on February 28, 2012. The senior secured credit facilities agreement allows for voluntary principal prepayments and requires mandatory principal prepayments within 90 days after calendar year-end based on a calculation of excess cash flow as defined in the senior secured credit facilities agreement. We repaid $10.0 million on the term loan facility on August 31, 2006 and $5.0 million on September 29, 2006. As of September 30, 2006, we had $44.6 million outstanding on the term loan facility. On October 31, 2006, we made a principal prepayment of $5.0 million.

In connection with obtaining the senior secured credit facilities, we incurred $2.5 million in debt issuance costs. These costs, which are recorded as a debt discount, are netted against the remaining principle amount outstanding. We will amortize these costs as interest expense over the term of the senior secured credit facilities agreement and will adjust such amortization for any prepayments on the term loan facility. During the nine months ended September 30, 2006, we amortized approximately $1.0 million as interest expense, including approximately $570,000 in additional interest expense associated with the acceleration in the amortization of the debt issuance costs due to the prepayments of debt principal in August and September 2006 totaling $15.0 million.

Under the terms of the senior secured credit facilities agreement, the credit facilities are guaranteed by all of our domestic subsidiaries and secured by perfected first priority security interests in, and mortgages on, substantially all of our tangible and intangible assets (including the capital stock of each specified subsidiary) and each of our subsidiaries. In addition, the facilities contain customary negative covenants applicable to us and our subsidiaries with respect to our operations and financial condition, such as a quarterly maximum twelve-month capital expenditure amount ($16.0 million for the twelve months ended September 30, 2006), a maximum interest coverage ratio as defined in the senior secured credit facilities agreement of 4.00 to 1.00 and a minimum leverage ratio as defined in the senior secured credit facilities agreement of 3.25 to 1.00.

We believe that our existing cash and cash equivalents, available borrowings and future cash provided by operating activities will be sufficient to meet our working capital and capital expenditure needs over the next 12 months. Our future capital requirements will depend on many factors, including our rate of revenue growth, the expansion of our marketing and sales activities, the timing and extent of spending to support product development efforts and expansion into new territories, the timing of introductions of new products or services, the timing of enhancements to existing products and services and the timing of capital expenditures. Also, we may make investments in, or acquisitions of, complementary businesses, services or technologies, which could also require us to seek additional equity or debt financing. To the extent that available funds are insufficient to fund our future activities, we may need to raise additional funds through public or private equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

We do not have any off-balance sheet arrangements with unconsolidated entities or related parties and accordingly, there are no off-balance sheet risks to our liquidity and capital resources from unconsolidated entities.

Quantitative and Qualitative Disclosures about Market Risk.

Our principal exposure to market risk relates to changes in interest rates. At September 30, 2006, $44.6 million was outstanding on our term loan facility with Credit Suisse, subject to covenants and restrictions. The interest rate on the term loan facility accrues at one of the following rates selected by us: (a) adjusted LIBOR plus 2.25%-2.50% or (b) an alternate base rate plus 1.25%-1.50%. The alternate base rate is the higher of Credit Suisse’s prime rate and the federal funds effective rate plus 0.5%. At September 30, 2006, the interest rate on the term loan facility was 7.57%. Interest rate changes would result in increases or decreases in the fair value of our debt due to differences between market interest rates and rates in effect at the inception of our debt obligation. For the three months ended September 30, 2006, a one percentage point increase in interest rates would have increased our interest expense by approximately $150,000.

Interest income on our cash and cash equivalents is subject to interest rate fluctuations. For the three months ended September 30, 2006, a one percentage point decrease in interest rates would have reduced our interest income by approximately $85,000.

We have accounts on our foreign subsidiaries ledgers which are maintained in the local foreign currency and remeasured into the United States Dollar. As a result, we are exposed to movements in the exchange rates of various currencies against the United States Dollar and against the currencies of other countries in which we sell products and services. In particular, we have accounts recorded in the Canadian Dollar. Therefore, when the Canadian Dollar strengthens or weakens against the United States Dollar, net income (loss) is increased or decreased, respectively. As a result, other expense of $301,000 was recorded during the nine months ended September 30, 2006.

Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures.

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2006. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of September 30, 2006, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) Changes in Internal Control over Financial Reporting.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended September 30, 2006 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Risk Factors.

Our merger with WebCT presents many risks, and we may not realize the financial and strategic goals that were contemplated at the time of the transaction.

The WebCT merger is the largest acquisition that we have undertaken. We entered into this transaction with the expectation that it would result in various benefits including, among other things, enhanced revenue and profits, and enhancements to our product portfolio and customer base. Risks that we may encounter in seeking to realize these benefits include:

- we may not realize the anticipated increase in our revenues if a larger than predicted number of customers decline to renew their contracts, if we are unable to sell WebCT's products to our customer base or if the acquired contracts do not allow us to recognize revenues on a timely basis;
- we may have difficulty incorporating WebCT's technologies or products with our existing product lines and maintaining uniform standards, controls, procedures and policies;
- we may have higher than anticipated costs in continuing support and development of WebCT's products;
- we may lose anticipated tax benefits or have additional legal or tax exposures;
- we may not be able to retain key WebCT employees;
- we may face contingencies related to product liability, intellectual property, financial disclosures, and accounting practices or internal controls; and
- we may be unable to manage effectively the increased size and complexity of the combined company, and our management's attention may be diverted from our ongoing business by transition or integration issues.

Our business strategy contemplates future business combinations and acquisitions which may be difficult to integrate, disrupt our business, dilute stockholder value or divert management attention.

During the course of our history, we have acquired several businesses, and a key element of our growth strategy is to pursue additional acquisitions in the future. Any acquisition could be expensive, disrupt our ongoing business and distract our management and employees. We may not be able to identify suitable acquisition candidates, and if we do identify suitable candidates, we may not be able to make these acquisitions on acceptable terms or at all. If we make an acquisition, we could have difficulty integrating the acquired technology, employees or operations. In addition, the key personnel of the acquired company may decide not to work for us. Acquisitions also involve the risk of potential unknown liabilities associated with the acquired business.

As a result of these risks, we may not be able to achieve the expected benefits of any acquisition. If we are unsuccessful in completing or integrating acquisitions that we may pursue in the future, we would be required to reevaluate our growth strategy, and we may have incurred substantial expenses and devoted significant management time and resources in seeking to complete and integrate the acquisitions.

Future business combinations could involve the acquisition of significant tangible and intangible assets, which could require us to record in our statements of operations ongoing amortization of intangible assets acquired in connection with acquisitions, which we currently do with respect to our historic acquisitions including the WebCT merger. In addition, we may need to record write-downs from future impairments of identified tangible and intangible assets and goodwill. These accounting charges would reduce any future reported earnings, or increase a reported loss. In future acquisitions, we could also incur debt to pay for acquisitions, or issue additional equity securities as consideration, which could cause our stockholders to suffer significant dilution.

Our ability to utilize, if any, net operating loss carryforwards acquired through the WebCT merger, or possibly any future acquisitions, may be significantly limited or unusable by us under Section 382 or other sections of the Internal Revenue Code.

We incurred a significant amount of debt to finance the WebCT merger, which could constrict our liquidity, result in substantial cash outflows, and adversely affect our financial health and ability to obtain financing in the future.

In connection with the WebCT merger, we secured $70.0 million in borrowings through Credit Suisse, Cayman Islands Branch consisting of a $60.0 million senior secured term loan facility repayable over six years and a $10.0 million senior secured revolving credit facility due and payable in full at the end of five years. This debt may impair our ability to obtain future additional financing for working capital, capital expenditures, acquisitions, general corporate or other purposes, and a substantial portion of our cash flows from operations may be dedicated to the debt repayment, thereby reducing the funds available to us for other purposes. This debt could make us more vulnerable to industry downturns and competitive pressures. Any failure by us to satisfy our obligations with respect to these debt obligations would constitute a default under the credit facilities. As of September 30, 2006, $44.6 million was outstanding under the term loan facility, and no amount was outstanding under the revolving credit facility. On October 31, 2006, we made a principal prepayment of $5.0 million.

Providing enterprise software applications to the education industry is an emerging and uncertain business; if the market for our products fails to develop, we will not be able to grow our business.

Our success will depend on our ability to generate revenues by providing enterprise software applications and services to colleges, universities, schools and other education providers. This market has only recently developed, and the viability and profitability of this market is unproven. Our ability to grow our business will be compromised if we do not develop and market products and services that achieve broad market acceptance with our current and potential clients and their students and employees. The use of online education, transactional or content management software applications and services in the education industry may not become widespread, and our products and services may not achieve commercial success. Even if potential clients decide to implement products of this type, they may still choose to design, develop or manage all or a part of their system internally.

Given our clients' relatively early adoption of enterprise software applications aimed at the education industry, they are likely to be less risk-averse than most colleges, universities, schools and other education providers. Accordingly, the rate at which we have been able to establish relationships with our clients in the past may not be indicative of the rate at which we will be able to establish additional client relationships in the future.

Most of our clients use our products to facilitate online education, which is a relatively new field; if online education does not continue to develop and gain acceptance, demand for our products could suffer.

Our success will depend in part upon the continued adoption by our clients and potential clients of online education initiatives. Some academics and educators are opposed to online education in principle and have expressed concerns regarding the perceived loss of control over the education process that can result from offering courses online. Some of these critics, particularly college and university professors, have the capacity to influence the market for online education, and their opposition could reduce the demand for our products and services. In addition, the growth and development of the market for online education may prompt some members of the academic community to advocate more stringent protection of intellectual property associated with course content, which may impose additional burdens on clients and potential clients offering online education. This could require us to modify our products, or could cause these clients and potential clients to abandon their online education initiatives.

We face intense and growing competition, which could result in price reductions, reduced operating margins and loss of market share.

We operate in highly competitive markets and generally encounter intense competition to win contracts. If we are unable to successfully compete for new business and license renewals, our revenue growth and operating margins may decline. The markets for online education, transactional, portal and content management products are intensely competitive and rapidly changing, and barriers to entry in these markets are relatively low. With the introduction of new technologies and market entrants, we expect competition to intensify in the future. Some of our principal competitors offer their products at a lower price, which has resulted in pricing pressures. Such pricing pressures and increased competition generally could result in reduced sales, reduced margins or the failure of our product and service offerings to achieve or maintain more widespread market acceptance.

Our primary competitors for the *Blackboard Academic Suite* are companies and open source solutions that provide course management systems, such as ANGEL Learning, Inc., Desire2Learn Inc., eCollege.com, Jenzabar, Inc., Moodle, The Sakai Project, VCampus Educator and WebTycho; learning content management systems, such as HarvestRoad Ltd. and Concord USA, Inc.; and education enterprise information portal technologies, such as SunGard SCT Inc., an operating unit of SunGard Data Systems Inc. We also face competition from clients and potential clients who develop their own applications internally, large diversified software vendors who offer products in numerous markets including the education market and other open source software applications. Our primary competitors for the *Blackboard Commerce Suite* are companies that provide university transaction systems, such as The CBORD Group, Inc., General Meters and NuVision Networks, as well as off-campus merchant relationship programs.

We may also face competition from potential competitors that are substantially larger than we are and have significantly greater financial, technical and marketing resources, and established, extensive direct and indirect channels of distribution. As a result, they may be able to respond more quickly to new or emerging technologies and changes in client requirements, or to devote greater resources to the development, promotion and sale of their products than we can. In addition, current and potential competitors have established or may establish cooperative relationships among themselves or prospective clients. Accordingly, it is possible that new competitors or alliances among competitors may emerge and rapidly acquire significant market share to our detriment.

If potential clients or competitors use open source software to develop products that are competitive with our products and services, we may face decreased demand and pressure to reduce the prices for our products.

The growing acceptance and prevalence of open source software may make it easier for competitors or potential competitors to develop software applications that compete with our products, or for clients and potential clients to internally develop software applications that they would otherwise have licensed from us. One of the aspects of open source software is that it can be modified or used to develop new software that competes with proprietary software applications, such as ours. Such competition can develop without the degree of overhead and lead time required by traditional proprietary software companies. As open source offerings become more prevalent, customers may defer or forego purchases of our products, which could reduce our sales and lengthen the sales cycle for our products or result in the loss of current clients to open source solutions. If we are unable to differentiate our products from competitive products based on open source software, demand for our products and services may decline, and we may face pressure to reduce the prices of our products.

Because most of our licenses are renewable on an annual basis, a reduction in our license renewal rate could significantly reduce our revenues.

Our clients have no obligation to renew their licenses for our products after the expiration of the initial license period, which is typically one year, and some clients have elected not to do so. A decline in license renewal rates could cause our revenues to decline. We have limited historical data with respect to rates of renewals, so we cannot accurately predict future renewal rates. Our license renewal rates may decline or fluctuate as a result of a number of factors, including client dissatisfaction with our products and services, our failure to update our products to maintain their attractiveness in the market or budgetary constraints or changes in budget priorities faced by our clients.

If our product development efforts, including our recently announced development effort codenamed Caliper, are delayed, fail to develop a product that gains market acceptance or fail to develop a marketable product at all, our financial results could suffer.

We may experience difficulties that could delay or prevent the successful development, introduction and sale of new products under development, such as our recently announced development effort codenamed Caliper. If introduced for sale, the new products may not adequately meet the requirements of the marketplace and may not achieve any significant degree of market acceptance, which could cause our financial results to suffer. In addition, during the development period for the new products, our customers may defer or forego purchases of our products and services.

Because we generally recognize revenues ratably over the term of our contract with a client, downturns or upturns in sales will not be fully reflected in our operating results until future periods.

We recognize most of our revenues from clients monthly over the terms of their agreements, which are typically 12 months, although terms can range from one month to 48 months. As a result, much of the revenue we report in each quarter is attributable to agreements entered into during previous quarters. Consequently, a decline in sales, client renewals, or market acceptance of our products in any one quarter will not necessarily be fully reflected in the revenues in that quarter, and will negatively affect our revenues and profitability in future quarters. This ratable revenue recognition also makes it difficult for us to rapidly increase our revenues through additional sales in any period, as revenues from new clients must be recognized over the applicable agreement term.

Our operating margins may suffer if our professional services revenues increase in proportion to total revenues because our professional services revenues have lower gross margins.

Because our professional services revenues typically have lower gross margins than our product revenues, an increase in the percentage of total revenues represented by professional services revenues could have a detrimental impact on our overall gross margins, and could adversely affect our operating results. In addition, we sometimes subcontract professional services to third parties, which further reduce our gross margins on these professional services. As a result, an increase in the percentage of professional services provided by third-party consultants could lower our overall gross margins.

If our products contain errors or if new product releases are delayed, we could lose new sales and be subject to significant liability claims.

Because our software products are complex, they may contain undetected errors or defects, known as bugs. Bugs can be detected at any point in a product's life cycle, but are more common when a new product is introduced or when new versions are released. In the past, we have encountered product development delays and defects in our products. We expect that, despite our testing, errors will be found in new products and product enhancements in the future. Significant errors in our products could lead to:

- delays in or loss of market acceptance of our products;
- diversion of our resources;
- a lower rate of license renewals or upgrades;
- injury to our reputation; and
- increased service expenses or payment of damages.

Because our clients use our products to store and retrieve critical information, we may be subject to significant liability claims if our products do not work properly. We cannot be certain that the limitations of liability set forth in our licenses and agreements would be enforceable or would otherwise protect us from liability for damages. A material liability claim against us, regardless of its merit or its outcome, could result in substantial costs, significantly harm our business reputation and divert management's attention from our operations.

The length and unpredictability of the sales cycle for our software could delay new sales and cause our revenues and cash flows for any given quarter to fail to meet our projections or market expectations.

The sales cycle between our initial contact with a potential client and the signing of a license with that client typically ranges from 6 to 15 months. As a result of this lengthy sales cycle, we have only a limited ability to forecast the timing of sales. A delay in or failure to complete license transactions could harm our business and financial results, and could cause our financial results to vary significantly from quarter to quarter. Our sales cycle varies widely, reflecting differences in our potential clients' decision-making processes, procurement requirements and budget cycles, and is subject to significant risks over which we have little or no control, including:

- clients' budgetary constraints and priorities;
- the timing of our clients' budget cycles;
- the need by some clients for lengthy evaluations that often include both their administrators and faculties; and
- the length and timing of clients' approval processes.

Potential clients typically conduct extensive and lengthy evaluations before committing to our products and services and generally require us to expend substantial time, effort and money educating them as to the value of our offerings.

Our sales cycle with international postsecondary education providers and U.S. K-12 schools may be longer than our historic U.S. postsecondary sales cycle, which could cause us to incur greater costs and could reduce our operating margins.

As we target more of our sales efforts at international postsecondary education providers and U.S. K-12 schools, we could face greater costs, longer sales cycles and less predictability in completing some of our sales, which may harm our business. In both of these markets, a potential client's decision to use our products and services may be a decision involving multiple institutions and, if so, these types of sales would require us to provide greater levels of education to prospective clients regarding the use and benefits of our products and services. In addition, we expect that potential clients in both of these markets may demand more customization, integration services and features. As a result of these factors, these sales opportunities may require us to devote greater sales support and professional services resources to individual sales, thereby increasing the costs and time required to complete sales and diverting sales and professional services resources to a smaller number of international and U.S. K-12 transactions.

We may have exposure to greater than anticipated tax liabilities.

We are subject to income taxes and other taxes in a variety of jurisdictions and are subject to review by both domestic and foreign taxation authorities. The determination of our provision for income taxes and other tax liabilities requires significant judgment and the ultimate tax outcome may differ from the amounts recorded in our consolidated financial statements, which may materially affect our financial results in the period or periods for which such determination is made.

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

Our federal net operating loss carryforwards are subject to limitations on how much may be utilized on an annual basis. The use of the net operating loss carryforwards may have additional limitations resulting from certain future ownership changes or other factors under Section 382 of the Internal Revenue Code.

If our net operating loss carryforwards are further limited, and we have taxable income which exceeds the available net operating loss carryforwards for that period, we would incur an income tax liability even though net operating loss carryforwards may be available in future years prior to their expiration, and our future cash flow, financial position and financial results may be negatively impacted.

Our future success depends on our ability to continue to retain and attract qualified employees.

Our future success depends upon the continued service of our key management, technical, sales and other critical personnel, including employees who joined Blackboard from WebCT. Whether we are able to execute effectively on our business strategy will depend in large part on how well key management and other personnel perform in their positions and are integrated within our company. Key personnel have left our company over the years, and there may be additional departures of key personnel from time to time. In addition, as we seek to expand our global organization, the hiring of qualified sales, technical and support personnel has been difficult due to the limited number of qualified professionals. Failure to attract, integrate and retain key personnel would result in disruptions to our operations, including adversely affecting the timeliness of product releases, the successful implementation and completion of company initiatives and the results of our operations.

If we do not maintain the compatibility of our products with third-party applications that our clients use in conjunction with our products, demand for our products could decline.

Our software applications can be used with a variety of third-party applications used by our clients to extend the functionality of our products, which we believe contributes to the attractiveness of our products in the market. If we are not able to maintain the compatibility of our products with third-party applications, demand for our products could decline, and we could lose sales. We may desire in the future to make our products compatible with new or existing third-party applications that achieve popularity within the education marketplace, and these third-party applications may not be compatible with our designs. Any failure on our part to modify our applications to ensure compatibility with such third-party applications would reduce demand for our products and services.

If we are unable to protect our proprietary technology and other rights, it will reduce our ability to compete for business.

If we are unable to protect our intellectual property, our competitors could use our intellectual property to market products similar to our products, which could decrease demand for our products. In addition, we may be unable to prevent the use of our products by persons who have not paid the required license fee, which could reduce our revenues. We rely on a combination of copyright, patent, trademark and trade secret laws, as well as licensing agreements, third-party nondisclosure agreements and other contractual provisions and technical measures, to protect our intellectual property rights. These protections may not be adequate to prevent our competitors from copying or reverse-engineering our products and these protections may be costly to enforce. Our competitors may independently develop technologies that are substantially equivalent or superior to our technology. To protect our trade secrets and other proprietary information, we require employees, consultants, advisors and collaborators to enter into confidentiality agreements. These agreements may not provide meaningful protection for our trade secrets, know-how or other proprietary information in the event of any unauthorized use, misappropriation or disclosure of such trade secrets, know-how or other proprietary information. The protective mechanisms we include in our products may not be sufficient to prevent unauthorized copying. Existing copyright laws afford only limited protection for our intellectual property rights and may not protect such rights in the event competitors independently develop products similar to ours. In addition, the laws of some countries in which our products are or may be licensed do not protect our products and intellectual property rights to the same extent as do the laws of the United States.

If we are found to infringe the proprietary rights of others, we could be required to redesign our products, pay significant royalties or enter into license agreements with third parties.

A third party may assert that our technology violates its intellectual property rights. As the number of products in our markets increases and the functionality of these products further overlaps, we believe that infringement claims will become more common. Any claims, regardless of their merit, could:

- be expensive and time consuming to defend;
- force us to stop licensing our products that incorporate the challenged intellectual property;
- require us to redesign our products and reimburse certain costs to our clients;
- divert management's attention and other company resources; and
- require us to enter into royalty or licensing agreements in order to obtain the right to use necessary technologies, which may not be available on terms acceptable to us, if at all.

Expansion of our business internationally will subject our business to additional economic and operational risks that could increase our costs and make it difficult for us to operate profitably.

One of our key growth strategies is to pursue international expansion. Expansion of our international operations may require significant expenditure of financial and management resources and result in increased administrative and compliance costs. As a result of such expansion, we will be increasingly subject to the risks inherent in conducting business internationally, including:

- foreign currency fluctuations, which could result in reduced revenues and increased operating expenses;
- potentially longer payment and sales cycles;
- difficulty in collecting accounts receivable;
- the effect of applicable foreign tax structures, including tax rates that may be higher than tax rates in the United States or taxes that may be duplicative of those imposed in the United States;
- tariffs and trade barriers;
- general economic and political conditions in each country;
- inadequate intellectual property protection in foreign countries;
- uncertainty regarding liability for information retrieved and replicated in foreign countries;
- the difficulties and increased expenses in complying with a variety of foreign laws, regulations and trade standards; and
- unexpected changes in regulatory requirements.

Unauthorized disclosure of data, whether through breach of our computer systems or otherwise, could expose us to protracted and costly litigation or cause us to lose clients.

Maintaining the security of online education and transaction networks is of critical importance for our clients because these activities involve the storage and transmission of proprietary and confidential client and student information, including personal student information and consumer financial data, such as credit card numbers, and this area is heavily regulated in many countries in which we operate, including the United States. Individuals and groups may develop and deploy viruses, worms and other malicious software programs that attack or attempt to infiltrate our products. If our security measures are breached as a result of third-party action, employee error, malfeasance or otherwise, we could be subject to liability or our business could be interrupted. Penetration of our network security could have a negative impact on our reputation and could lead our present and potential clients to choose competing offerings and result in regulatory action against us. Even if we do not encounter a security breach ourselves, a well-publicized breach of the consumer data security of any major consumer Web site could lead to a general public loss of confidence in the use of the Internet, which could significantly diminish the attractiveness of our products and services.

Operational failures in our network infrastructure could disrupt our remote hosting service, could cause us to lose current hosting clients and sales to potential hosting clients and could result in increased expenses and reduced revenues.

Unanticipated problems affecting our network systems could cause interruptions or delays in the delivery of the hosting service we provide to some of our clients. We provide remote hosting through computer hardware that is currently located in third-party co-location facilities in Virginia, The Netherlands and Canada. We do not control the operation of these co-location facilities. Lengthy interruptions in our hosting service could be caused by the occurrence of a natural disaster, power loss, vandalism or other telecommunications problems at the co-location facilities or if these co-location facilities were to close without adequate notice. Although we have multiple transmission lines into the co-location facilities through two telecommunications service providers, we have experienced problems of this nature from time to time in the past, and we will continue to be exposed to the risk of network failures in the future. We currently do not have adequate computer hardware and systems to provide alternative service for most of our hosted clients in the event of an extended loss of service at the co-location facilities. Each Virginia co-location facility provides data backup redundancy for the other Virginia co-location facility. However, they are not equipped to provide full disaster recovery to all of our hosted clients. If there are operational failures in our network infrastructure that cause interruptions, slower response times, loss of data or extended loss of service for our remotely hosted clients, we may be required to issue credits or pay penalties, current hosting clients may terminate their contracts or elect not to renew them, and we may lose sales to potential hosting clients. If we determine that we need additional hardware and systems, we may be required to make further investments in our network infrastructure.

We could lose revenues if there are changes in the spending policies or budget priorities for government funding of colleges, universities, schools and other education providers.

Most of our clients and potential clients are colleges, universities, schools and other education providers who depend substantially on government funding. Accordingly, any general decrease, delay or change in federal, state or local funding for colleges, universities, schools and other education providers could cause our current and potential clients to reduce their purchases of our products and services, to exercise their right to terminate licenses, or to decide not to renew licenses, any of which could cause us to lose revenues. In addition, a specific reduction in governmental funding support for products such as ours would also cause us to lose revenues.

U.S. and foreign government regulation of the Internet could cause us to incur significant expenses, and failure to comply with applicable regulations could make our business less efficient or even impossible.

The application of existing laws and regulations potentially applicable to the Internet, including regulations relating to issues such as privacy, defamation, pricing, advertising, taxation, consumer protection, content regulation, quality of products and services and intellectual property ownership and infringement, can be unclear. It is possible that U.S., state and foreign governments might attempt to regulate Internet transmissions or prosecute us for violations of their laws. In addition, these laws may be modified and new laws may be enacted in the future, which could increase the costs of regulatory compliance for us or force us to change our business practices. Any existing or new legislation applicable to us could expose us to substantial liability, including significant expenses necessary to comply with such laws and regulations, and dampen the growth in use of the Internet.

Specific federal laws that could also have an impact on our business include the following:

- The Children's Online Protection Act and the Children's Online Privacy Protection Act restrict the distribution of certain materials deemed harmful to children and impose additional restrictions on the ability of online services to collect personal information from children under the age of 13; and
- The Family Educational Rights and Privacy Act imposes parental or student consent requirements for specified disclosures of student information, including online information.

Our clients' use of our software as their central platform for online education initiatives may make us subject to any such laws or regulations, which could impose significant additional costs on our business or subject us to additional liabilities.

We may be subject to state and federal financial services regulation, and any violation of any present or future regulation could expose us to liability, force us to change our business practices or force us to stop selling or modify our products and services.

Our transaction processing product and service offering could be subject to state and federal financial services regulation. The *Blackboard Transaction System* supports the creation and management of student debit accounts and the processing of payments against those accounts for both on-campus vendors and off-campus merchants. For example, one or more federal or state governmental agencies that regulate or monitor banks or other types of providers of electronic commerce services may conclude that we are engaged in banking or other financial services activities that are regulated by the Federal Reserve under the U.S. Federal Electronic Funds Transfer Act or

Regulation E thereunder or by state agencies under similar state statutes or regulations. Regulatory requirements may include, for example:

- disclosure of consumer rights and our business policies and practices;
- restrictions on uses and disclosures of customer information;
- error resolution procedures;
- limitations on consumers' liability for unauthorized account activity;
- data security requirements;
- government registration; and
- reporting and documentation requirements.

A number of states have enacted legislation regulating check sellers, money transmitters or transaction settlement service providers as banks. If we were deemed to be in violation of any current or future regulations, we could be exposed to financial liability and adverse publicity or forced to change our business practices or stop selling some of our products and services. As a result, we could face significant legal fees, delays in extending our product and services offerings, and damage to our reputation that could harm our business and reduce demand for our products and services. Even if we are not required to change our business practices, we could be required to obtain licenses or regulatory approvals that could cause us to incur substantial costs.

Exhibits.

(a) Exhibits:

Exhibit No.	Description
10 .1	Employment Agreement between the Registrant and Michael Beach dated September 1, 2006.
10 .2	Employment Agreement between the Registrant and Peter Segall dated September 1, 2006.
31 .1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31 .2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32 .1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32 .2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURE

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.

Blackboard Inc.

By: /s/ Michael J. Beach

Michael J. Beach

Chief Financial Officer

(On behalf of the registrant and as Principal Financial Officer)

Dated: November 9, 2006

Exhibit 10.1

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the “**Agreement**”) is entered into by and between Michael Beach (“**you**”) and Blackboard Inc. (“ **Blackboard** ”).

WHEREAS, Blackboard desires to continue to employ you on the terms and conditions hereinafter set forth and you desire to accept such employment;

NOW, THEREFORE, in consideration of the promises and the mutual agreements contained herein, the parties agree as follows:

1. Responsibilities. Blackboard agrees to hire you as the Chief Financial Officer. You shall devote your entire business time, attention, skill and energy exclusively to the business of Blackboard and perform the responsibilities assigned to you in accordance with the standards and policies that Blackboard may from time to time establish. You may engage in appropriate civic or charitable activities and devote a reasonable amount of time to private investments or boards or other activities provided that such activities do not interfere or conflict with your responsibilities and are not or are not likely to be contrary to Blackboard’s interests. You and Blackboard agree that your position is essential to Blackboard’s success and that the highest level of performance is required from you.

2. Term of Employment. Blackboard agrees to employ you, and you agree to remain in employment with Blackboard, from September 1, 2006 until August 31, 2007 (the “ **Initial Term** ”), unless your employment terminates earlier pursuant to Section 5 below. This Agreement shall automatically renew for successive one (1) year periods (each, a “ **Renewal Term** ” and together with the Initial Term, the “ **Term** ”) unless either party provides prior written notice of its intent not to renew at least thirty (30) days prior to the first day of the applicable Renewal Term.

3. Compensation.

(a) Base Compensation. Your annual base compensation shall initially be US$260,000 (“**Base Compensation**”), less applicable taxes and withholdings, payable in accordance with Blackboard’s regular payroll practices from time to time in effect. Blackboard’s Board of Directors (the “ **Board** ”) may review and adjust your Base Compensation periodically.

(b) Bonus Compensation. To be eligible to receive an annual bonus for any year, you must meet financial performance targets set by the Board and be employed through March 31st of the following year. Your initial target bonus shall be 50% of your Base Compensation. The actual amount of the bonus, if any, will be determined by the Board in its sole discretion (the “Bonus”). If a Bonus is awarded, it will be paid in the year following that for which the Bonus is being awarded. You will be eligible for your first bonus under this Agreement for a pro rated portion of 2006, if any, in 2007 as approved by the Board.

(c) Business Expenses. During the Term, Blackboard shall pay or reimburse you for all ordinary and reasonable business-related expenses you incur in the performance of your duties under this Agreement. Blackboard will reimburse you for all such expenses upon the presentation by you of an itemized account of such expenditures, together with supporting receipts and other appropriate documentation.

4. Employee Benefits.

(a) In General. During the Term, you shall be eligible for all employee benefits that Blackboard may provide to employees who are officers of Blackboard, which may include, but are not limited to benefits such as health insurance plans, a stock option plan, paid holidays and 401(k), subject in each case to the generally applicable terms and conditions of any such plan or program in question and to the determinations of any person or committee administering any such plan or program. Blackboard reserves the right to modify or terminate any such benefit at any time.

(b) Vacation. You shall be eligible to take paid vacation during each calendar year in accordance with Blackboard’s Employment Handbook.

5. Termination of Employment. Upon the effective date of termination of your employment with Blackboard (the “**Termination Date** ”), you will not be eligible for further compensation, benefits or perquisites under Sections 3 and 4

of this Agreement, other than those that have already accrued or vested as of the Termination Date. Termination of your employment may occur under any of the following circumstances:

(a) Expiration of Term. Your employment will terminate if the Term provided for under Section 2 expires pursuant to the notice requirements of Section 2; or

(b) Termination of Employment by Blackboard. Blackboard has the right to terminate your employment at any time with or without Cause. For all purposes under this Agreement, (“ **Cause** ”) shall mean:

(i) non-feasance or your material breach of this Agreement, provided that Blackboard first provides you with written notice of such failure and you fail to cure it within ten (10) days of such notice;

(ii) an act or omission by you that constitutes gross misconduct, moral turpitude or fraud;

(iii) a conviction for, or a plea of “guilty” or “no contest” to, a felony; or

(iv) a material breach of any legally recognized duty owed to Blackboard (e.g., your duty of loyalty and confidentiality).

(c) Resignation by You. You have the right to resign your employment with Blackboard at any time, with or without Good Reason, provided that you may resign with Good Reason only if you provide notice of such reason for resignation to Blackboard stating that such reason will be grounds for resignation with Good Reason, and if Blackboard fails to cure such reason within thirty (30) days following receipt of such notice.

(i) For purposes of this Agreement, “**Good Reason**” shall mean (A) a material failure by Blackboard to perform its obligations under this Agreement; (B) your relocation outside of your current residential area without your consent; (C) a material diminution of your compensation, duties or responsibilities at any time or for any reason other than for Cause during the Term of this Agreement; or (D) failure to renew this Agreement pursuant to Section 2.

(ii) During the Term, you agree to provide Blackboard ninety (90) days’ prior written notice of your resignation, with or without Good Reason. Blackboard may in its sole discretion place you on paid administrative leave as of any date prior to the end of such ninety (90) day notice period and request that you no longer be present on Blackboard premises. During any period of paid administrative leave, you will not be authorized to act as a representative, or make any statements on behalf of, Blackboard; or

(d) Death or Disability. Your employment shall be deemed to have been terminated by you upon your (i) death or (ii) inability to perform your duties under this Agreement, even with reasonable accommodation, for more than twenty-six (26) weeks, whether or not consecutive, in any twelve-month period (“ **Disability** ”). Termination will be effective upon the occurrence of such event.

6. Severance Payments.

If during the Term of this Agreement, Blackboard terminates your employment without Cause (as defined in Section 5(b)) or you resign for Good Reason and comply with the obligations set forth in Section 5(c), then Blackboard will pay you your then current Base Salary, less applicable taxes and withholdings, for twelve (12) months (“ **Severance Payments** ”). The Severance Payments shall be made consistent with Blackboard’s regular payroll schedule. If you timely apply and qualify for COBRA, Blackboard will pay your COBRA premiums, at your current level of coverage, for twelve (12) months, unless you become covered by another employer’s health insurance, in which case the COBRA coverage will be terminated when your new coverage commences. You agree to notify Blackboard immediately if you become covered by another employer’s health insurance plan. To receive the Severance Payments and COBRA premiums you must sign a release of any and all claims in the form provided by Blackboard. Such Severance Payments and COBRA premiums shall begin at the later of (i) the first pay period following your Termination Date or (ii) ten (10) days after you deliver the signed release to Blackboard.

7. Return of Property. Upon termination of your employment with Blackboard for any reason, you agree to immediately return to Blackboard all equipment, credit cards and other property belonging to Blackboard. This includes all documents and other information prepared by you or on your behalf or provided to you in connection with performing your duties for Blackboard, regardless of the form in which such documents or information are maintained or stored, including computer, typed, written, imaged, audio, video, micro-fiche, electronic or any other means of recording or storing documents or other information. You hereby warrant that you will not retain in any form any such document or other information or copies thereof, except as provided in the following sentence. You may retain a copy of any documents describing any rights or obligations you may have after the Termination Date under any employee benefit plan or other agreements.

8. Confidentiality, Non-Solicitation and Non-Competition Agreement.

(a) Confidential Information. You shall not disclose or use at any time, either during your employment or after your Termination Date, any confidential information, including, but not limited to, the terms of this Agreement, existing and prospective investments, trade secrets or proprietary information, strategic sourcing information or analysis, financing information and sources, patents, patent applications, developmental or experimental work, formulas, test data, prototypes, models, know how and product specifications, financial information, financial projections and pro forma financial information, sales and marketing strategies, plans and programs and product development information, employees' and consultants' benefits, perquisites, salaries, stock options, compensation, formulas or bonuses, and their non-business addresses and telephone numbers, organizational structure and reporting relationships, business plans, names, addresses, phone numbers of customers, contracts, including contracts with clients, suppliers, independent contractors or employees, business plans and forecasts, and existing and prospective projects or business opportunities (" **Confidential Information** ") of Blackboard, whether patentable or not, which you learn as a result of your employment with Blackboard, whether or not you developed such information. **"Confidential Information"** shall not include, without limitation, information that is or later becomes publicly available in a manner wholly unrelated to any breach of this Agreement by you as of the date it enters the public domain. If you are uncertain whether something is Confidential Information you should treat it as Confidential Information until you receive clarification from Blackboard that it is not Confidential Information. Confidential Information shall remain at all times the property of Blackboard. You may use or disclose Confidential Information only as authorized and necessary in performing your responsibilities under this Agreement during your employment with Blackboard; with the General Counsel's prior written consent; in a legal proceeding between you and Blackboard to establish the rights of either party under this Agreement, provided that you stipulate to a protective order to prevent any unnecessary use or disclosure; or subject to a compulsory legal process that requires disclosure of such information, provided that you have complied with the following procedures to ensure that Blackboard has an adequate opportunity to protect its legal interests in preventing disclosure. Upon receipt of a subpoena that could possibly require disclosure of Confidential Information, you shall provide a copy of the compulsory process and complete information regarding the circumstances under which you received it to Blackboard by hand delivery within twenty-four (24) hours. You will not make any disclosure until the latest possible date for making such disclosure in accordance with the compulsory process (" **Latest Possible Date** "). If Blackboard seeks to prevent disclosure in accordance with the applicable legal procedures, and provides you with notice before the Latest Possible Date that it has initiated such procedures, you will not make disclosures of any Confidential Information that is the subject of such procedures, until such objections are withdrawn or ruled on. You hereby acknowledge that any breach of this Section 8(a) would cause Blackboard irreparable harm.

(b) Outside Activities. You shall submit to Blackboard's General Counsel, within a reasonable time prior to dissemination, the text of any speech, professional paper, article or similar communication created by you which relates to Blackboard's present or future business or research and development endeavors. The General Counsel then will notify you if the dissemination of the communication is permitted under the terms of this Agreement.

(c) Ownership of Confidential Information; Return of Materials. All Confidential Information, including without limitation that which is produced by or for Blackboard by you or anyone else, all materials embodying Confidential Information, and all copies thereof, will remain the property of Blackboard or of the third party who has furnished it to Blackboard. On your Termination Date, or at the written request of Blackboard at any time, you will immediately deliver to Blackboard all materials, and copies thereof, which are in your possession or control and which contain or are related in any way to any Confidential Information. This includes all documents and other information prepared by you or on your behalf or provided to you in connection with your duties while employed by Blackboard, regardless of the form in which such document or information are maintained or stored, including computer, typed, written, imaged, audio, video, micro-fiche, electronic or any other means of recording or storing documents or other information. You hereby warrant that you will not retain in any form any such document or other information or copies thereof. You may retain a copy of this Agreement and any other document or information describing any rights you may have after the termination of your employment.

(d) Intellectual Property.

(i) For purposes of this Agreement the following terms will be defined as indicated:

(A) "**Inventions**" shall mean inventions, ideas, formula, developments, designs, systems, software, discoveries, and improvements to existing technology, whether or not patentable.

(B) "**Improvements**" shall mean all inventions, developments, modifications, changes, whether or not patentable, made to any Inventions and/or Confidential Information.

(C) "**Copyrighted Work**" shall mean any work of authorship eligible for copyright protection under the federal and state laws of the United States and foreign countries.

(D) "**Copyrights**" shall mean any and all rights granted in Copyrighted Works under the laws of the United States and foreign countries.

(ii) Exclusions. An Invention, Copyright or Copyrighted Work will not be subject to this Agreement when all the following criteria are met: (A) no equipment, supplies, facilities, or Confidential Information of Blackboard was used in developing the Invention or Copyrighted Work or in applying for or obtaining a patent or Copyright; (B) the Invention or Copyrighted Work was developed entirely on your own time; (C) the Invention or Copyrighted Work does not relate directly to the business of Blackboard or to Blackboard's actual or demonstrably anticipated research or development; and (D) the Invention, Copyright or Copyrighted Work does not result from any work performed by you for Blackboard or at the request of Blackboard.

(iii) Ownership and Assignment of Rights.

(A) All Inventions, Improvements, or Confidential Information that you have or will conceive or develop, either alone or with others, shall be the exclusive property of Blackboard. You hereby assign, and agree to assign, to Blackboard your entire right, title, and interest in and to (I) any and all such Improvements and Inventions, (II) any and all applications for patent, domestic and foreign that may be filed on said Improvements and Inventions, and (III) any and all patents that may issue or be granted on such applications, except those excluded under Section 8(d)(ii) of this Agreement. Both during your employment and after your Termination Date you will on request immediately sign and deliver to Blackboard without further consideration any and all documents necessary to perfect the assignments granted in this Section.

(B) You understand and agree that all Copyrighted Works conceived, developed, created or contributed to by you shall be considered works made for hire under the copyright laws of the United States and shall be the exclusive property of Blackboard. Blackboard shall be considered the author of such Copyrighted Works. You further understand and agree that in the event any Copyrighted Work created by you within the scope of, or in connection with, your work with Blackboard, or at the request of Blackboard, fails to meet the legal requirements of a work made for hire owned by Blackboard, then this Agreement shall operate to assign to Blackboard all of your rights, title, and interest, including copyrights, in, to and under such Copyrighted Works. Blackboard shall have sole and absolute discretion to register, enforce, and/or assign Copyrights for such Copyrighted Works.

(iv) Assistance and Designation of Agent.

(A) Both during your employment and after your Termination Date, you will on request immediately sign and deliver to Blackboard without further consideration, all instruments in writing requiring your signature and deemed by Blackboard to be necessary or advisable in, or in connection with, filing or prosecuting of any application for any patent covering Improvements, Inventions or any divisional, continuing, renewal or reissue application or reexamination request based upon any application for patent. In the event that Blackboard is unable for any reason whatsoever to secure your signature to any lawful and necessary documents required to apply for or execute any patent application with respect to such idea, process, development, design, system, program, discovery, invention, improvement or writing (including renewals, extensions, continuations, divisions or continuations in part thereof), you hereby irrevocably designate and appoint Blackboard and its officers and agents, as your agents and attorneys-in-fact to act for and on your behalf and instead of you, to execute and file any such application and to do all other lawfully permitted acts to further the prosecution and issuance of patents thereon with the same legal force and effect as if executed by you.

(B) You will aid Blackboard promptly on request, and without further consideration, in any matter pertaining to or relating to the protection of any of the Improvements, Inventions, applications for patents covering Inventions or Improvements, and/or Copyrighted Works. If such request is made after your employment has ended, Blackboard will reimburse you for any expenses incurred and compensate for any services rendered in complying with such request at the same rate at which you were compensated during the final month of your employment.

9. Non-Solicitation/Non-Competition.

During your employment and for one (1) year following your Termination Date (the "**Restricted Period**") you will not, except with prior written approval of Blackboard's General Counsel, directly or indirectly, individually or as part of or on behalf of any other person, company, employer or other entity: (a) hire or attempt to solicit for hire, or encourage to end their relationship with Blackboard, any persons who have been employed by Blackboard at any time within the previous six (6) months (a " **Covered Employee** "); (b) sell or otherwise provide, or solicit for the purposes of selling or otherwise providing, services or products that are similar or related to those sold by Blackboard as of the Termination Date to any person or entity that has within the twelve (12) months preceding the Termination Date purchased any such services or products from Blackboard and with whom you had direct contact on behalf of Blackboard during that time; or (c) own, manage, operate, control, be employed by, participate in, work in, advise, consult or contract with, or support in any manner any business that is similar to the type of business conducted by Blackboard as of the Termination Date within the geographical area in which, as of the Termination Date, Blackboard is actively marketing or has made a significant investment in time and money to prepare to market its products or services within the six (6) month period after the Termination Date. You agree that these provisions are necessary to protect Blackboard's legitimate business interests. You warrant that the provisions will not unreasonably interfere in your ability to earn a living or to pursue your occupation after the Termination Date. You agree to notify any person or entity to which you provide services during the Restricted Period of your obligations under this Section 9.

10. Non-Disparagement. You agree to refrain from making any derogatory or defamatory remarks or comments that may disparage Blackboard, or any officer, employee or agent of Blackboard during your employment or after your Termination Date.

11. Other Obligations. You warrant that you are not subject to any other obligations that would conflict with or inhibit your ability to perform your duties under this Agreement. You represent that you have disclosed to Blackboard the existence and contents of all covenants not to compete that you have entered into with any other entity. You further warrant that you have not and will not bring to Blackboard or use in the performance of your responsibilities at Blackboard any equipment, supplies, facility or trade secret information (that is not generally available to the public) of any current or former employer or organization other than Blackboard to which you provided services, unless you have obtained written authorization for their possession and use.

12. Miscellaneous Provisions.

(a) Notices. Unless otherwise provided herein, any notice or other communication required to be given under the terms of this Agreement must be in writing and must be personally delivered (i.e., left with an individual 18 years of age or older) or sent by overnight delivery. Documents sent by overnight delivery will be presumed received on the next business day following the day sent.

If notice is to be sent to Blackboard, it will be sent to:

Matthew Small, Esq.
Blackboard Inc
1899 L Street, N.W., 5th Floor
Washington DC 20036

With a copy to:

Douglas B. Mishkin, Esq.
Patton Boggs, LLP
2550 M Street, NW
Washington, DC 20037

If notice is to be sent to you, it will be sent to:

Michael Beach

____
____

(b) Dispute Resolution. You and Blackboard agree that any dispute between you and Blackboard will be finally resolved by binding arbitration in accordance with the Federal Arbitration Act (" **FAA** "). You and Blackboard agree to follow the Dispute Resolution Procedures set forth in **Attachment A** to this Agreement.

(c) Nature of Agreement. This Agreement and the attachment hereto constitute the entire agreement between you and Blackboard and supersede all prior agreements and understandings between you and Blackboard relating to the matters covered by this Agreement, except for the existing stock option agreements between you and Blackboard, which remain in full force and effect. Any long-term equity incentives between Blackboard and you shall be contained in a separate agreement. In making this Agreement, the parties warrant that they did not rely on any representations or statements other than those contained in this Agreement. No modification of or amendment to this Agreement will be effective unless in writing and signed by the General Counsel or Senior Vice President for Human Resources of Blackboard. A delay or failure by Blackboard to exercise any right that is the subject of this Agreement will not be construed as a waiver of that right. A waiver of a breach on any one occasion will not be construed as a waiver of any other breach. Regardless of the choice of law or conflict of law provisions of the District of Columbia or any other jurisdiction, the parties agree that this Agreement shall be otherwise interpreted, enforced and governed by the laws of the District of Columbia. This Agreement will continue in effect until all obligations under it are fulfilled. If any part of this Agreement is held by a court of competent jurisdiction to be void or unenforceable, the remaining provisions shall continue with full force and effect. This Agreement is not assignable by you. This Agreement is binding on you with respect to Blackboard, its successors or assigns. This Agreement may be executed in any number of counterparts each of which shall be an original, but all of which together shall constitute one instrument. The headings in this Agreement are for convenience only and shall not effect the interpretation of this Agreement. You further certify that you fully understand the terms of this Agreement and have entered into it knowingly and voluntarily.

IN WITNESS WHEREOF, each of the parties has executed this Agreement, in the case of Blackboard by its authorized officer, as of the day and year set forth under their signatures below.

/s/ Michael Beach
Michael Beach

Date: 9/1/2006

Blackboard Inc.

By: /s/ Michael Chasen
Michael Chasen, CEO and President

Date: 9/1/2006

Attachment A

DISPUTE RESOLUTION PROCEDURES

The parties agree to make a good faith effort to informally resolve any dispute before submitting the dispute to arbitration in accordance with the following procedures:

A. The party claiming to be aggrieved shall furnish to the other a written statement of the grievance, all persons whose testimony would support the grievance, and the relief requested or proposed. The written statements must be delivered to the other party within the time limits for bringing an administrative or court action based on that claim.

B. If the other party does not agree to furnish the relief requested or proposed, or otherwise does not satisfy the demand of the party claiming to be aggrieved within thirty (30) days and the aggrieved party wishes to pursue the issue, the aggrieved party shall by written notice demand that the dispute be submitted to non-binding mediation before a mediator jointly selected by the parties.

C. If mediation does not produce a resolution of the dispute and either party wishes to pursue the issue, that party shall request arbitration of the dispute by giving written notice to the other party within thirty (30) days after mediation. The parties will attempt to agree on a mutually acceptable arbitrator and, if no agreement is reached, the parties will follow the procedures established by the JAMS Employment Arbitration Rules and Procedures ("Rules"), which may be found at www.jamsadr.com/rules/employment_arbitration_Rules.asp. The arbitration will be conducted consistent with JAMS/Endispute's rules governing employment disputes (" **Rules** ") that are in effect at the time of the arbitration. If there is any conflict between those Rules and the terms of the Employment Agreement (" **Agreement** "), including all attachments thereto, the Agreement will govern. The arbitrator shall have the authority to decide whether the conduct complained of under Subsection A above violates the legal rights of the parties. In any such arbitration proceeding, any hearing must be transcribed by a certified court reporter and any decision must be supported by written findings of fact and conclusions of law. The arbitrator's findings of fact must be supported by substantial evidence on the record as a whole and the conclusions of law and any remedy must be provided for by and consistent with the laws of District of Columbia and federal law. The arbitrator shall have no authority to add to, modify, change or disregard any lawful term of the Agreement. Blackboard will pay the arbitrator's fee. The arbitrator's decision will be final and binding on Blackboard and you and may be recorded as a judgment in a court of competent jurisdiction.

D. Arbitration shall be the exclusive means for final resolution of any dispute between the parties, except (1) for workers' compensation and unemployment claims and (2) when injunctive relief is necessary to preserve the status quo or to prevent irreparable injury, including, without limitation, any claims concerning an alleged or threatened breach of your obligations regarding confidentiality, non-solicitation and non-competition. Injunctive relief may be sought from any court of competent jurisdiction located in the District of Columbia.

Exhibit 10.2

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the "**Agreement**") is entered into by and between Peter Segall ("**you**") and Blackboard Inc. (" **Blackboard** ") and is effective as of September 1, 2006.

WHEREAS, Blackboard desires to employ you on the terms and conditions hereinafter set forth and you desire to accept such employment;

NOW, THEREFORE, in consideration of the promises and the mutual agreements contained herein, the parties agree as follows:

1. Responsibilities. Blackboard agrees to employ you as the President of U.S. Higher Education. You shall report to Blackboard's CEO and shall be a member of Blackboard's Senior Executive Committee. You shall devote your entire business time, attention, skill and energy exclusively to the business of Blackboard and perform the responsibilities assigned to you in accordance with the standards and policies that Blackboard may from time to time establish. You may engage in appropriate civic or charitable activities and devote a reasonable amount of time to private investments or boards or other activities provided that such activities do not interfere or conflict with your responsibilities and are not or are not likely to be contrary to Blackboard's interests. You and Blackboard agree that your position is essential to Blackboard's success and that the highest level of performance is required from you.

2. Term of Employment. Blackboard agrees to employ you, and you agree to remain in employment with Blackboard, from September 1, 2006 until August 31, 2007 (the " **Initial Term** "), unless your employment terminates earlier pursuant to Section 5 below. This Agreement shall automatically renew for successive one (1) year periods (each, a " **Renewal Term** " and together with the Initial Term, the " **Term** ") unless either party provides prior written notice of its intent not to renew. You must provide notice of your intent not to renew at least ninety (90) days prior the first day of the applicable Renewal Term and Blackboard must provide notice of its intent not to renew at least thirty (30) days' prior to the first day of the applicable Renewal Term.

3. Compensation.

(a) Base Compensation. Your annual base compensation shall initially be US$250,000 ("**Base Compensation**"), less applicable taxes and withholdings, payable in accordance with Blackboard's regular payroll practices from time to time in effect. Blackboard's Board of Directors (the " **Board** ") may review and adjust your Base Compensation periodically.

(b) Bonus Compensation. Your initial target bonus will be up to 50% of your Base Compensation. The actual amount of the bonus, if any, will be determined by the Board in its sole discretion. If a bonus is awarded, it will be paid in the year following that for which the bonus is being awarded. To be eligible to receive an annual bonus for any fiscal year, you must meet financial performance targets set by the Board and be employed through March 31st of the following year.

For 2006, you will earn a pro-rated portion of $90,000 corresponding to the period between January 1, 2006 and the date hereof. You will also be eligible to earn a pro rated portion of your 2006 bonus for the time period beginning September 1, 2006 through December 31, 2006, which will be calculated in the same or similar manner to other executive employees.

(c) Business Expenses. During the Term, Blackboard shall pay or reimburse you for all ordinary and reasonable business-related expenses you incur in the performance of your duties under this Agreement. Blackboard will reimburse you for all such expenses, in accordance with its policies and procedures, upon the presentation by you of an itemized account of such expenditures, together with supporting receipts and other appropriate documentation.

4. Employee Benefits.

(a) In General. During the Term, you shall be eligible for all employee benefits that Blackboard may provide to employees who are officers of Blackboard, which may include, but are not limited to benefits such as health insurance plans, a stock option plan, paid holidays and 401(k), subject in each case to the generally applicable terms and conditions of any such plan or program in question and to the determinations of any person or committee administering any such plan or program. Blackboard reserves the right to modify or terminate any such benefit at any time.

(b) Vacation. You shall be eligible to take paid vacation during each calendar year in accordance with Blackboard's Employment Handbook.

(c) Corporate Housing. Blackboard will have the option to either provide you with use of an apartment in the Washington, DC area, beginning on September 1, 2006 for the Term of this Agreement or to reimburse you for the reasonable cost of rent for such an apartment.

5. Termination of Employment. Upon the effective date of termination of your employment with Blackboard (the "**Termination Date** "), you will not be eligible for further compensation, benefits or perquisites under Sections 3 and 4 of this Agreement, other than those that have already accrued or vested as of the Termination Date. Termination of your employment may occur under any of the following circumstances:

(a) Expiration of Term. Your employment will terminate if the Term provided for under Section 2 expires pursuant to the notice requirements of Section 2; or

(b) Termination of Employment by Blackboard. Blackboard has the right to terminate your employment at any time with or without Cause. For all purposes under this Agreement, (" **Cause** ") shall mean:

(i) willful failure to observe the material, standard published policies of Blackboard or to carry out the reasonable and proper directives of the Board, consistent with the Employee's position and duties under this Agreement;

(ii) willful misconduct or gross negligence by the Employee in respect of his obligations to the Company;

(iii) a conviction of, or a plea of nolo contendere by, the Employee of a felony involving moral turpitude;

(iv) a material violation or breach of the terms of this Agreement; or

(v) theft of the property of Blackboard or other disloyal or dishonest conduct of the Employee that materially harms the Company or its business.

(c) Resignation by You. You have the right to resign your employment with Blackboard at any time, with or without Good Reason, provided that you may resign with Good Reason only if you provide notice of such reason for resignation to Blackboard stating that such reason will be grounds for resignation with Good Reason, and if Blackboard fails to cure such reason within thirty (30) days following receipt of such notice.

(i) For purposes of this Agreement, "**Good Reason**" shall mean (A) a material failure by Blackboard to perform its obligations under this Agreement; (B) your relocation to more than 50 miles outside of your residence (at the time of your execution of this Agreement) without your consent; or (C) a material diminution of your compensation, duties or responsibilities.

(ii) During the Term, you agree to provide Blackboard ninety (90) days' prior written notice of your resignation, with or without Good Reason. Blackboard may in its sole discretion place you on paid administrative leave as of any date prior to the end of such ninety (90) day notice period and request that you no longer be present on Blackboard premises. During any period of paid administrative leave, you will not be authorized to act as a representative, or make any statements on behalf of, Blackboard; or

(d) Death or Disability. Your employment shall be deemed to have been terminated by you upon your (i) death or (ii) inability to perform your duties under this Agreement, even with reasonable accommodation, for more than twenty-six (26) weeks, whether or not consecutive, in any twelve-month period (" **Disability** "). Termination will be effective upon the occurrence of such event.

6. Severance Payments.

If (i) Blackboard terminates your employment without Cause (as defined in Section 5(b)) at any time during the Term, or (ii) you resign for Good Reason and comply with the obligations set forth in Section 5(c), or (iii) you resign for any reason during the eighteen (18) month period immediately following your execution of this Agreement and provide ninety (90) days' notice of such resignation, then Blackboard will pay you your then current Base Salary, less applicable taxes and withholdings, for twelve (12) months (" **Severance Payments** "). If, following the end of a calendar year but prior to receiving your bonus for the completed calendar year, you are terminated without Cause or resign for Good Reason, you shall also receive your bonus, less taxes and withholdings, for the completed calendar year as part of the Severance Payments at such time as the Board deems appropriate, consistent with the payment of the other executives' bonuses. The Severance Payments shall be made consistent with Blackboard's regular payroll schedule and paid monthly for twelve (12) months or in a lump sum at Blackboard's discretion. If you timely apply and qualify for COBRA, Blackboard will pay your COBRA premiums, at your current level of coverage, for twelve (12) months, unless you become covered by another employer's health insurance, in which case the COBRA coverage will be terminated when your new coverage commences. You agree to notify Blackboard immediately if you become covered by another employer's health insurance plan. To receive the Severance Payments and COBRA premiums you must sign a release of any and all claims in the form provided by Blackboard. Such Severance Payments and COBRA premiums shall begin at the later of (i) the first pay period following your Termination Date or (ii) ten (10) days after you deliver the signed release to Blackboard.

7. Return of Property. Upon termination of your employment with Blackboard for any reason, you agree to immediately return to Blackboard all equipment, credit cards and other property belonging to Blackboard. This includes all documents and other information prepared by you or on your behalf or provided to you in connection with performing your duties for Blackboard, regardless of the form in which such documents or information are maintained or stored, including computer, typed, written, imaged, audio, video, micro-fiche, electronic or any other means of recording or storing documents or other information. You hereby warrant that you will not retain in any form any such document or other information or copies thereof, except as provided in the following sentence. You may retain a copy of any documents describing any rights or obligations you may have after the Termination Date under any employee benefit plan or other agreements.

8. Confidentiality, Non-Solicitation and Non-Competition Agreement.

(a) Confidential Information. You shall not disclose or use at any time, either during your employment or after your Termination Date, any confidential information, including, but not limited to, the terms of this Agreement, existing and prospective investments, trade secrets or proprietary information, strategic sourcing information or analysis, financing information and sources, patents, patent applications, developmental or experimental work, formulas, test data, prototypes, models, know how and product specifications, financial information, financial projections and pro forma financial information, sales and marketing strategies, plans and programs and product development information, employees' and consultants' benefits, perquisites, salaries, stock options, compensation, formulas or bonuses, and their non-business addresses and telephone numbers, organizational structure and reporting relationships, business plans, names, addresses, phone numbers of customers, contracts, including contracts with clients, suppliers, independent contractors or employees, business plans and forecasts, and existing and prospective projects or business opportunities (" **Confidential Information** ") of Blackboard, whether patentable or not, which you learn as a result of your employment with Blackboard, whether or not you developed such information. **"Confidential Information"** shall not include, without limitation, information that is or later becomes publicly available in a manner wholly unrelated to any breach of this Agreement by you as of the date it enters the public domain or information that is already in your possession prior to your receipt of it from the Company and which is not the subject of an obligation of confidence of any kind.

If you are uncertain whether something is Confidential Information you should treat it as Confidential Information until you receive clarification from Blackboard that it is not Confidential Information. Confidential Information shall remain at all times the property of Blackboard. You may use or disclose Confidential Information only as authorized and necessary in performing your responsibilities under this Agreement during your employment with Blackboard; with the General Counsel's prior written consent; in a legal proceeding between you and Blackboard to establish the rights of either party under this Agreement, provided that you stipulate to a protective order to prevent any unnecessary use or disclosure; or subject to a compulsory legal process that requires disclosure of such information, provided that you have complied with the following procedures to ensure that Blackboard has an adequate opportunity to protect its legal interests in preventing disclosure. Upon receipt of a subpoena that could possibly require disclosure of Confidential Information, you shall provide a copy of the compulsory process and complete information regarding the circumstances under which you received it to Blackboard by hand delivery within twenty-four (24) hours. You will not make any disclosure until the latest possible date for making such disclosure in accordance with the compulsory process (" **Latest Possible Date** "). If Blackboard seeks to prevent disclosure in accordance with the applicable legal procedures, and provides you with notice before the Latest Possible Date that it has initiated such procedures, you will not make disclosures of any Confidential Information that is the subject of such procedures, until such objections are withdrawn or ruled on. You hereby acknowledge that any breach of this Section 8(a) would cause Blackboard irreparable harm.

(b) Outside Activities. You shall submit to Blackboard's General Counsel, within a reasonable time prior to dissemination, the text of any speech, professional paper, article or similar communication created by you which relates to Blackboard's present or future business or research and development endeavors. The General Counsel then will notify you if the dissemination of the communication is permitted under the terms of this Agreement.

(c) Ownership of Confidential Information; Return of Materials. All Confidential Information, including without limitation that which is produced by or for Blackboard by you or anyone else, all materials embodying Confidential Information, and all copies thereof, will remain the property of Blackboard or of the third party who has furnished it to Blackboard. On your Termination Date, or at the written request of Blackboard at any time, you will immediately deliver to Blackboard all materials, and copies thereof, which are in your possession or control and which contain or are related in any way to any Confidential Information. This includes all documents and other information prepared by you or on your behalf or provided to you in connection with your duties while employed by Blackboard, regardless of the form in which such document or information are maintained or stored, including computer, typed, written, imaged, audio, video, micro-fiche, electronic or any other means of recording or storing documents or other information. You hereby warrant that you will not retain in any form any such document or other information or copies thereof. You may retain a copy of this Agreement and any other document or information describing any rights you may have after the termination of your employment.

(d) Intellectual Property.

(i) For purposes of this Agreement the following terms will be defined as indicated:

(A) "**Inventions**" shall mean inventions, ideas, formula, developments, designs, systems, software, discoveries, and improvements to existing technology, whether or not patentable.

(B) "**Improvements**" shall mean all inventions, developments, modifications, changes, whether or not patentable, made to any Inventions and/or Confidential Information.

(C) "**Copyrighted Work**" shall mean any work of authorship eligible for copyright protection under the federal and state laws of the United States and foreign countries.

(D) "**Copyrights**" shall mean any and all rights granted in Copyrighted Works under the laws of the United States and foreign countries.

(ii) Exclusions. An Invention, Copyright or Copyrighted Work will not be subject to this Agreement when all the following criteria are met: (A) no equipment, supplies, facilities, or Confidential Information of Blackboard was used in developing the Invention or Copyrighted Work or in applying for or obtaining a patent or Copyright; (B) the Invention or Copyrighted Work was developed entirely on your own time; (C) the Invention or Copyrighted Work does not relate directly to the business of Blackboard or to Blackboard's actual or demonstrably anticipated research or development; and (D) the Invention, Copyright or Copyrighted Work does not result from any work performed by you for Blackboard or at the request of Blackboard.

(iii) Ownership and Assignment of Rights.

(A) All Inventions, Improvements, or Confidential Information that you have or will conceive or develop, either alone or with others, shall be the exclusive property of Blackboard. You hereby assign, and agree to assign, to Blackboard your entire right, title, and interest in and to (I) any and all such Improvements and

Inventions, (II) any and all applications for patent, domestic and foreign that may be filed on said Improvements and Inventions, and (III) any and all patents that may issue or be granted on such applications, except those excluded under Section 8(d)(ii) of this Agreement. Both during your employment and after your Termination Date you will on request immediately sign and deliver to Blackboard without further consideration any and all documents necessary to perfect the assignments granted in this Section.

(B) You understand and agree that all Copyrighted Works conceived, developed, created or contributed to by you shall be considered works made for hire under the copyright laws of the United States and shall be the exclusive property of Blackboard. Blackboard shall be considered the author of such Copyrighted Works. You further understand and agree that in the event any Copyrighted Work created by you within the scope of, or in connection with, your work with Blackboard, or at the request of Blackboard, fails to meet the legal requirements of a work made for hire owned by Blackboard, then this Agreement shall operate to assign to Blackboard all of your rights, title, and interest, including copyrights, in, to and under such Copyrighted Works. Blackboard shall have sole and absolute discretion to register, enforce, and/or assign Copyrights for such Copyrighted Works.

(iv) Assistance and Designation of Agent.

(A) Both during your employment and after your Termination Date, you will on request immediately sign and deliver to Blackboard without further consideration, all instruments in writing requiring your signature and deemed by Blackboard to be necessary or advisable in, or in connection with, filing or prosecuting of any application for any patent covering Improvements, Inventions or any divisional, continuing, renewal or reissue application or reexamination request based upon any application for patent. In the event that Blackboard is unable for any reason whatsoever to secure your signature to any lawful and necessary documents required to apply for or execute any patent application with respect to such idea, process, development, design, system, program, discovery, invention, improvement or writing (including renewals, extensions, continuations, divisions or continuations in part thereof), you hereby irrevocably designate and appoint Blackboard and its officers and agents, as your agents and attorneys-in-fact to act for and on your behalf and instead of you, to execute and file any such application and to do all other lawfully permitted acts to further the prosecution and issuance of patents thereon with the same legal force and effect as if executed by you.

(B) You will aid Blackboard promptly on request, and without further consideration, in any matter pertaining to or relating to the protection of any of the Improvements, Inventions, applications for patents covering Inventions or Improvements, and/or Copyrighted Works. If such request is made after your employment has ended, Blackboard will reimburse you for any expenses incurred and compensate for any services rendered in complying with such request at the same rate at which you were compensated during the final month of your employment.

9. Non-Solicitation/Non-Competition.

During your employment and for two (2) years following your Termination Date (the "**Restricted Period**") you will not, except with prior written approval of Blackboard's General Counsel, directly or indirectly, individually or as part of or on behalf of any other person, company, employer or other entity: (a) hire or attempt to solicit for hire, or encourage to end their relationship with Blackboard, any persons who have been employed by Blackboard at any time within the previous six (6) months (a " **Covered Employee** "); (b) sell or otherwise provide, or solicit for the purposes of selling or otherwise providing, services or products that are similar or related to those sold by Blackboard as of the Termination Date to any person or entity that has within the twelve (12) months preceding the Termination Date purchased any such services or products from Blackboard and with whom you had direct contact on behalf of Blackboard during that time; or (c) own, manage, operate, control, be employed by, participate in, work in, advise, consult or contract with, or support in any manner (other than as the holder of not more than one percent (1%) of the total outstanding stock of a publicly held company) any business that is similar to the type of business conducted by Blackboard as of the Termination Date within the geographical area in which, as of the Termination Date, Blackboard is actively marketing or has made a significant investment in time and money to prepare to market its products or services within the six (6) month period after the Termination Date. You agree that these provisions are necessary to protect Blackboard's legitimate business interests. You warrant that the provisions will not unreasonably interfere in your ability to earn a living or to pursue your occupation after the Termination Date. You agree to notify any person or entity to which you provide services during the Restricted Period of your obligations under this Section 9.

10. Non-Disparagement. You agree to refrain from making any derogatory or defamatory remarks or comments that may disparage Blackboard, or any officer, employee or agent of Blackboard during your employment or after your Termination Date.

11. Other Obligations. You warrant that you are not subject to any other obligations that would conflict with or inhibit your ability to perform your duties under this Agreement. You represent that you have disclosed to Blackboard the existence and contents of all covenants not to compete that you have entered into with any other entity. You further warrant that you have not and will not bring to Blackboard or use in the performance of your responsibilities at Blackboard any equipment, supplies, facility or trade secret information (that is not generally available to the public) of any current or former employer or organization other than Blackboard to which you provided services, unless you have obtained written authorization for their possession and use.

12. Miscellaneous Provisions.

(a) Notices. Unless otherwise provided herein, any notice or other communication required to be given under the terms of this Agreement must be in writing and must be personally delivered (i.e., left with an individual 18 years of age or older) or sent by overnight delivery. Documents sent by overnight delivery will be presumed received on the next business day following the day sent.

If notice is to be sent to Blackboard, it will be sent to:

Matthew Small, Esq.
Blackboard Inc.
1899 L Street, N.W., 5th Floor
Washington DC 20036

With a copy to:

Douglas B. Mishkin, Esq.
Patton Boggs, LLP
2550 M Street, NW
Washington, DC 20037

If notice is to be sent to you, it will be sent to:

(b) Dispute Resolution. You and Blackboard agree that any dispute between you and Blackboard will be finally resolved by binding arbitration in accordance with the Federal Arbitration Act (“ **FAA** ”). You and Blackboard agree to follow the Dispute Resolution Procedures set forth in **Attachment A** to this Agreement.

(c) Nature of Agreement. This Agreement and the attachment hereto constitute the entire agreement between you and Blackboard and supersede all prior agreements and understandings between you and Blackboard relating to the matters covered by this Agreement, including your prior Employment Agreement dated October 31, 2002, as amended, which is hereby terminated in all respects. Any long-term equity incentives between Blackboard and you shall be contained in a separate agreement. In making this Agreement, the parties warrant that they did not rely on any representations or statements other than those contained in this Agreement. No modification of or amendment to this Agreement will be effective unless in writing and signed by the General Counsel or Senior Vice President for Human Resources of Blackboard. A delay or failure by either party to exercise any right that is the subject of this Agreement will not be construed as a waiver of that right. A waiver of a breach on any one occasion will not be construed as a waiver of any other breach. Regardless of the choice of law or conflict of law provisions of the District of Columbia or any other jurisdiction, the parties agree that this Agreement shall be otherwise interpreted, enforced and governed by the laws of the District of Columbia. This Agreement will continue in effect until all obligations under it are fulfilled. If any part of this Agreement is held by a court of competent jurisdiction to be void or unenforceable, the remaining provisions shall continue with full force and effect. This Agreement is not assignable by you. This Agreement is binding on you with respect to Blackboard, its successors or assigns. This Agreement may be executed in any number of counterparts each of which shall be an original, but all of which together shall constitute one instrument. The headings in this Agreement are for convenience only and shall not effect the interpretation of this Agreement. You further certify that you fully understand the terms of this Agreement and have entered into it knowingly and voluntarily.

IN WITNESS WHEREOF, each of the parties has executed this Agreement, in the case of Blackboard by its authorized officer, as of the day and year set forth under their signatures below.

	Blackboard Inc.
/s/ Peter Segall	By: /s/ Michael Chasen
Peter Segall	Michael Chasen, CEO and President
Date: September 1, 2006	Date: September 1, 2006

<u>Attachment A</u>

DISPUTE RESOLUTION PROCEDURES

The parties agree to make a good faith effort to informally resolve any dispute before submitting the dispute to arbitration in accordance with the following procedures:

A. The party claiming to be aggrieved shall furnish to the other a written statement of the grievance, all persons whose testimony would support the grievance, and the relief requested or proposed. The written statements must be delivered to the other party within the time limits for bringing an administrative or court action based on that claim.

B. If the other party does not agree to furnish the relief requested or proposed, or otherwise does not satisfy the demand of the party claiming to be aggrieved within thirty (30) days and the aggrieved party wishes to pursue the issue, the aggrieved party shall by written notice demand that the dispute be submitted to non-binding mediation before a mediator jointly selected by the parties.

C. If mediation does not produce a resolution of the dispute and either party wishes to pursue the issue, that party shall request arbitration of the dispute by giving written notice to the other party within thirty (30) days after mediation. The parties will attempt to agree on a mutually acceptable arbitrator and, if no agreement is reached, the parties will follow the procedures established by the JAMS Employment Arbitration Rules and Procedures ("Rules"), which may be found at www.jamsadr.com/rules/employment_arbitration_Rules.asp. The arbitration will be conducted consistent with JAMS/Endispute's rules governing employment disputes (" **Rules** ") that are in effect at the time of the arbitration. If there is any conflict between those Rules and the terms of the Employment Agreement (" **Agreement** "), including all attachments thereto, the Agreement will govern. The arbitrator shall have the authority to decide whether the conduct complained of under Subsection A above violates the legal rights of the parties. In any such arbitration proceeding, any hearing must be transcribed by a certified court reporter and any decision must be supported by written findings of fact and conclusions of law. The arbitrator's findings of fact must be supported by substantial evidence on the record as a whole and the conclusions of law and any remedy must be provided for by and consistent with the laws of District of Columbia and federal law. The arbitrator shall have no authority to add to, modify, change or disregard any lawful term of the Agreement. Blackboard will pay the arbitrator's fee. Each party will bear its own attorneys' fees and costs, unless the arbitrator orders the award of attorneys' fees and costs. The arbitrator's decision will be final and binding on Blackboard and you and may be recorded as a judgment in a court of competent jurisdiction.

D. Arbitration shall be the exclusive means for final resolution of any dispute between the parties, except (1) for workers' compensation and unemployment claims and (2) when injunctive relief is necessary to preserve the status quo or to prevent irreparable injury, including, without limitation, any claims concerning an alleged or threatened breach of your obligations regarding confidentiality, non-solicitation and non-competition. Injunctive relief may be sought from any court of competent jurisdiction located in the District of Columbia.

EXHIBIT 31.1

Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Michael L. Chasen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Blackboard Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: November 9, 2006

/s/ Michael L. Chasen
Michael L. Chasen
Chief Executive Officer

EXHIBIT 31.2

Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Michael J. Beach, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Blackboard Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: November 9, 2006

/s/ Michael J. Beach
Michael J. Beach
Chief Financial Officer

EXHIBIT 32.1

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

I, Michael L. Chasen, Chief Executive Officer of Blackboard Inc. (the “Company”), do hereby certify, under the standards set forth in and solely for the purposes of 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge that:

1. The Quarterly Report on Form 10-Q of the Company for the period ended September 30, 2006 (the “Quarterly Report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as amended; and

2. The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 9, 2006

/s/ Michael L. Chasen
Michael L. Chasen
Chief Executive Officer

EXHIBIT 32.2

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

I, Michael J. Beach, Chief Financial Officer of Blackboard Inc. (the "Company"), do hereby certify, under the standards set forth in and solely for the purposes of 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge that:

1. The Quarterly Report on Form 10-Q of the Company for the period ended September 30, 2006 (the "Quarterly Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as amended; and
2. The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 9, 2006

/s/ Michael J. Beach
Michael J. Beach
Chief Financial Officer