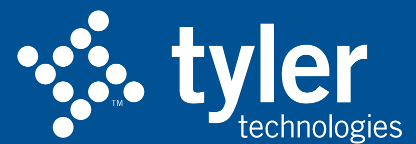
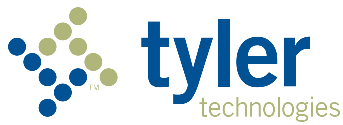
Speaking from Experience



2009 Annual Report

On the cover from left to right:

Ken Miles, Courts & Justice Solutions
Melissa Baer, Appraisal & Property Tax Solutions
Mandye Perez, Public Safety Solutions



Empowering people who serve the public™

Every day, Tyler Technologies draws from our many years of experience to empower the people who serve the public. With best-in-class software solutions and deep domain expertise, Tyler helps local governments and schools manage their many complex operations—including financial management, property appraisal and assessment, school administration, court case management and law enforcement. Following an outstanding financial performance in 2008, Tyler once again grew revenues and earnings in 2009, delivering solid results for our shareholders, clients and employees.

To Our Shareholders

Tyler Technologies' performance in 2009 demonstrated how our business strategy was designed to perform in all economic environments. During a challenging recession year, we made meaningful progress under our long-term plans while growing both revenues and earnings.

At Tyler, we have a unique vantage point due to our singular focus on serving the public sector with a broad product portfolio. From financial management and property taxes to courts and education, we create, deliver and support software solutions that make it easier for local governments and schools to manage their complex, day-to-day business functions. Tyler knows how to develop and support innovative software solutions for the market. We also have an insider's insight to the market, as many of Tyler's employees worked in the public sector prior to joining our team. With this knowledge and experience—along with focused innovation and an earnest commitment to our clients—we are positioned better than anyone to anticipate and address the changing technology needs of the public sector.

However, our commitment goes well beyond delivering solutions that work for our public sector clients. It's about consistently delivering value for employees and shareholders as well. Building on a successful foundation, Tyler continues to provide a solid return for shareholders. We remained committed to our long-term growth strategies even through a challenging financial climate and ended 2009 in a position of strength.

In 2009, Tyler was once again recognized for its business performance and leadership, as well as being honored as a top place to work. For the third straight year, *Forbes* named Tyler Technologies as one of "America's 200 Best Small Companies." In addition, Tyler was recognized as one of the "Best Places to Work in Maine," as well as one of "*The Dallas Morning News* Top 100 Places to Work 2009."

Making Meaningful Progress

In a difficult economic climate that saw many software companies struggle, Tyler Technologies was still able to make progress, both financially and strategically. We ended 2009 with 35 consecutive quarters of profitability. Tyler closed the year with total revenue of $290.3 million, up 10 percent from 2008. Gross margins increased 300 basis points to 44.4 percent, and our operating margin reached a new high of 15.4 percent. Earnings per diluted share totaled $0.74, and increased 21 percent over non-GAAP EPS for 2008, even as we continued to invest aggressively in product development and competitive initiatives.

Although Tyler achieved improved financial results by almost every meaningful measure, our growth has clearly been affected by the broader economic environment and by pressures on local government budgets. While our significant base of recurring revenues (now comprising approximately half of total revenues) combined with the mission-critical nature of our solutions provides us with a great deal of stability, we experienced lengthened sales cycles throughout the year. New request for proposal activity continues to support a very healthy sales pipeline. However, the timing of contract signings and revenue recognition is less predictable, as many local governments' purchasing processes are longer and more complex than in a more favorable economic environment.

Tyler was once again recognized for its business performance and leadership, as well as being honored as a top place to work by our employees.

In 2009, we experienced another year of strong cash flow generation, with total free cash flow of $40 million (excluding capital expenditures for office construction). We rely on this strong free

cash flow to make strategic investments that will further strengthen our position for the future, while enhancing shareholder value. We also repurchased $17 million of our common stock and completed several acquisitions to augment our appraisal and property tax and schools solutions.

Given our consistent growth, significant recurring revenues, healthy cash flow and strong market reputation, Tyler is in an excellent position to build upon its competitive strengths as we move into 2010 and beyond.

Speaking from our many years of experience, Tyler empowers local governments and schools, and consistently delivers a solid return for shareholders. And it is with this experience that we move into 2010 with confidence in and commitment to our long-term opportunities and strategies.

Building Lasting Success

While many competitors target multiple vertical markets, Tyler has a singular focus—delivering essential software solutions that empower the public sector. And unlike many of our competitors that serve only a narrow niche of the public sector, we offer what we believe is the broadest range of software and solutions for local governments and schools.

From the courtroom to the classroom, Tyler's solutions serve as the backbone for core business functions. We devote all of our time, energy and resources to helping local governments and school districts streamline the many aspects of their financial management, court case, property tax, public safety, citizen services, public records and education systems.

While the timing of public sector investments in technology is clearly affected by the economy, the fact remains that the functions Tyler automates are essential to our clients, and our solutions enable them to operate more efficiently, doing more with less.

Tyler's success follows a carefully designed business plan that focuses on four key strategies: expanding geographically, broadening our product offerings, securing larger opportunities, and extending our relationships with existing clients. As we look forward to 2010 and beyond, we intend to continue building upon these long-term strategies.

Creating a Stronger Identity

Since the late 1990s, Tyler has shown consistent organic growth at above market rates—augmenting its market strength through targeted acquisitions. While this has afforded us the ability to broaden our product offerings and penetrate new markets, these acquisitions have also posed some challenges.

As expected, each acquired business had its own identity, strategy and approach to sales and marketing—not to mention its own unique way of interfacing with clients. As these business units and products were integrated into the company, Tyler worked hard to create a unified corporate identity—bringing together strong products with long-standing reputations—under the Tyler name.

In 2009, we launched a wide-scale rebranding effort to further strengthen Tyler's identity and position in the public sector—a historically fragmented market. A cohesive identity allows us to build a stronger competitive advantage for Tyler to capture even more market share and build greater awareness as the leader in public sector software. And through new communication channels and branding efforts, we are also generating a renewed sense of energy and enthusiasm among Tyler employees and clients across all product groups.

Investing in the Future

Throughout 2009, Tyler Technologies again demonstrated that success requires the right combination of many factors—a well-designed strategy, consistent execution, feature-rich and industry-proven products, talented employees and a solid brand identity. Underscoring each of these components is the one fundamental question: how can we empower the people who serve the public?

For us, the simplest answer is to develop, implement, and support software solutions that deliver—again and again. For our clients, this means delivering the right types of systems to address their many complex needs. For our shareholders, this translates to delivering a solid return on their investment now and over the long term. And for our employees, this means fostering the right work environment—one that encourages them to innovate, create, and achieve success personally and professionally.

At Tyler, we consider research and development an essential investment in our future. And in 2009—at a time when many companies chose, or were forced, to reduce discretionary spending for R&D and cut staff—Tyler aggressively invested in product development and added to our team.

In addition to investing in product updates to enhance functionality and integrate new features and technologies in our existing products, Tyler has devoted substantial resources to the development of new products that we believe will provide meaningful growth opportunities in the future. This includes Microsoft Dynamics AX, a business management solution for the public sector that we are co-developing with Microsoft. During the fourth quarter of 2009, we expanded the scope of our multi-year arrangement with Microsoft, adding payroll, human resources, and budget formulation applications to the solution. In 2009, we also secured our first "beta" client for Microsoft Dynamics AX—with a general release slated for early 2011.

Moving Forward

Although 2009 presented a challenging economic climate that we expect to continue in 2010, Tyler Technologies had a solid year in terms of financial performance. Looking to the future, it is our hope that 2010 will be a year of economic recovery for the marketplace, providing Tyler a healthy mix of opportunity and challenge. Given our strong market position and rich history of proven success, we are confident in our ability to generate reasonable results in difficult times—while continuing to invest in initiatives that we believe will put us in an even stronger competitive position as the market returns to more normal conditions.

Tyler empowers local governments and schools, and consistently delivers a solid return for shareholders. And it is with this experience that we move into 2010 with confidence in and commitment to our long-term opportunities and strategies.

John S. Marr, Jr.
President and Chief Executive Officer

Donna Martindale and John White
ERP/Financial Solutions

Speaking the Same Language. There's a certain familiarity and comfort in sharing a common language with your clients—something Donna Martindale and John White understand firsthand. Both John and Donna were early adopters of Tyler products long before they ever joined the company as employees. When he went to work for the Town of Shrewsbury, Massachusetts, John had the rare opportunity to design a town-wide information system from the ground up. During this process, Tyler's financial management solution was selected for implementation. Today, as senior solution consultant at Tyler, John is still sharing his expertise to help local governments realize the full power of Tyler's financial management solutions. Like John, Donna was also a Tyler financial management solution end-user while in her role as finance director for Harker Heights, Texas. And for the past 12 years, Donna has been helping local governments migrate to Tyler as an implementation manager. "I sit with a client and can relate to them," Donna explains. "I can tell them 'I did your job.' It's so incredible that I'm able to hand off a tool to our clients—a tool that empowers them to make a real change in their city."

Empowering the Public Sector

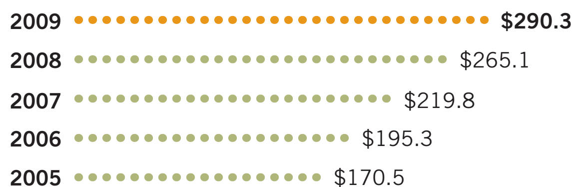
During a time when many companies have struggled, Tyler Technologies has proven itself as a market leader. Drawing from our years of experience, Tyler posted another successful year in 2009—even in the midst of a turbulent economy.

Tyler delivers software and services solutions that enable city, county and state agencies of all sizes to efficiently and effectively manage their day-to-day business operations. In fact, no other company offers as wide a range of products as Tyler.

Today, Tyler has more than 9,000 client installations in all 50 states, Puerto Rico, the U.S. Virgin Islands, Canada and the United Kingdom. Thanks to Tyler's exceptional flexibility and comprehensive product portfolio, we are competitive at every level—from small rural communities to large metropolitan areas and statewide implementations. We have the financial strength and resources of a large company, yet we can act with the agility and ingenuity of an innovative entrepreneurial organization committed to building lasting relationships with our clients.

Many people don't appreciate the challenges that local governments and schools face in providing numerous mission-critical services every day—from routing school buses and managing jails to collecting taxes and paying firemen. To effectively oversee these activities, public sector organizations must have robust technology platforms available around the clock.

Total Annual Revenues
(In Millions)



> Tyler Technologies' consistent, long-term success is the result of singularly focusing on serving the public sector, creating a sound vision, and executing our growth strategy with precision.

Yet, like many private sector businesses today, local governments are increasingly facing pressure to be more efficient and more productive using fewer resources. Thus, governments must make smarter business decisions based on the needs of their agencies and the citizens they serve.

From our years of experience in serving the public sector, Tyler understands that delivering software solutions that help our clients efficiently manage their many operations is just the beginning. Harnessing the true power and potential of Tyler's product offerings—solutions backed by our highly experienced team—is realized through long-term partnerships with our clients.

That's why Tyler's relationship with clients goes well beyond merely that of a vendor. We act as a trusted partner for local governments. It is this commitment that has helped us maintain an approximately 98 percent customer retention rate for many years. In fact, many of our first clients are still with Tyler today. With a deep understanding of how local governments operate, Tyler is well positioned to deliver solutions that address these unique needs now—and well into the future.

Building a Strong Foundation

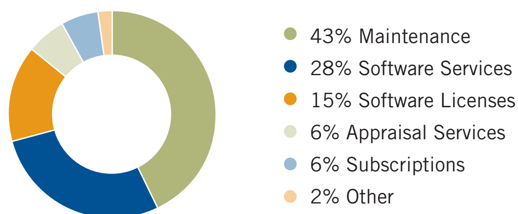
As communities throughout the United States experience growth and face changes in budgets, demographics and technology, local governments must have the right systems in place to handle citizens' evolving needs and demands—from parental access to student grades to the convenience of paying traffic tickets and utility bills online.

With Tyler's performance in 2009, we have once again illustrated that focusing exclusively on one vertical market offers ample room for long-term growth. In fact, there are approximately 3,000 counties, 13,900 school districts, 36,000 cities and towns, and more than 35,000 other local government agencies in the United States alone—each with multiple software systems. We believe that the majority of these systems are either "in-house" solutions or were purchased from vendors that are no longer competitive in the market—presenting great opportunities for Tyler to gain market share as these systems are replaced over the coming years.

In 2009, Tyler increased revenues by 10 percent, more than doubling the estimated market growth in a sluggish economy. Additionally, our recurring revenues from maintenance and subscriptions increased by 16 percent, and now make up almost half of our total revenues. This creates a solid base of reliable revenues on which we can build sustainable growth.

Backlog
(In Millions)

Revenue Mix



Tyler Technologies experienced solid growth in key areas throughout 2009—and we will continue to build upon this foundation in the years to come.

Throughout the year, Tyler experienced a reasonable, although not robust, level of new business activity, creating a healthy pipeline of new business. However, longer sales cycles and delayed decision processes made the timing of new business less predictable. We ended 2009 with a total backlog of signed contracts of $233 million, down modestly from the end of 2008. Our backlog, combined with highly reliable recurring revenues, provides us with a high degree of visibility into our expected revenues.

While Tyler has continued to refine our growth strategy over the years, in 2009, we focused primarily on the same core initiatives—moving into new geographic areas, expanding our product offerings, securing larger contracts, and cross-selling additional products and services to existing clients. And in refreshing our brand identity in 2009, we now have a more cohesive product portfolio under the Tyler name—helping us further solidify our position as the go-to leader for software solutions within the public sector.

Innovating for Tomorrow

As Tyler has grown over the years, our market has matured as well. While there are fewer competitors now than a decade ago, there are always good companies vying with Tyler for market share. To stay competitive in this vertical market, it's essential that Tyler stay at the forefront of innovation. Only then can we deliver the types of robust solutions local governments and schools need—when they need them.

At Tyler, we believe this starts by having the best possible team in place. Tyler now has more than 2,000 professionals who bring unmatched expertise

Johnnie Gordon, Amy Puckett and John Mathis
Courts & Justice Solutions

Speaking from Authority. From minor traffic citations to major criminal trials, courts and justice offices at the state, county and municipal level face a tremendous task of streamlining critical information. "The most important thing is first understanding their business processes, so we can help them make the most out of their software environment," explains Johnnie Gordon, who was a courts and justice consultant prior to joining Tyler as a regional project manager for Tyler's courts & justice solutions. Like Johnnie, developer John Mathis spent many years in the public sector, including positions such as a system administrator for Denton County, Texas. He came on board at Tyler in 1994, and today develops the tools and functionality courts and justice offices rely on to serve their constituents. Having this level of insight has also been invaluable for Amy Puckett who, like John, served in various roles for Denton County—including emergency dispatcher and detention officer. For the past 18 years, she has helped courts and justice offices fine-tune their processes as a product manager. "At the end of the day, there's simply no substitute for this experience," says Johnnie. "To me, what we do is more than just deliver software—it's about bringing value to courts and justice offices and the people they serve through the experience and firsthand knowledge we have gained over the years."

Melissa Belec, Marsha Craft and Larry Frazier
School Solutions

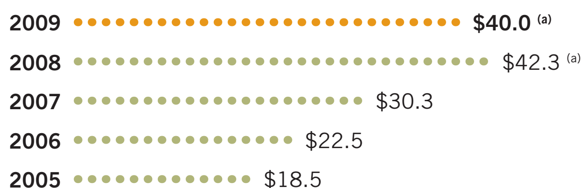
Speaking from Support. Fortunately, there are people like Larry Frazier, Marsha Craft and Melissa Belec who work behind the scenes to empower school personnel. "Some people know the software, but it helps that I also know schools," comments Larry, who held positions as a teacher, a principal and a technology coordinator prior to becoming an implementation analyst for Tyler. "My experience makes it easier for me to help school districts use our school solutions to work more efficiently." Like Larry, Marsha Craft is no stranger to educating others. As a senior trainer, she helps school district personnel realize the full power and potential of Tyler's products. She brings the in-depth experience of her 35-year career—15 of those years spent serving in a student information system role in a growing Missouri school district—to help clients navigate changes, address key issues and share best practices. Marketing Program Specialist Melissa Belec understands the advantage in having a client's perspective. "I was a hands-on user of Tyler's student transportation solutions for three years in a school district," explains Melissa, who later joined Tyler in product and technical support before moving into a marketing role. "I can speak their language and I understand their issues, which really makes a big difference."

in technology development and deployment, as well as a deep understanding of how our clients operate. In fact, many of our employees held positions in the public sector prior to joining Tyler, providing a firsthand understanding of the many nuances of how local governments and schools work from day to day.

Some of our competitors reduced their workforce and cut expenditures in research and development last year in response to the recession. However, Tyler's strong cash flow and above-market growth throughout the year enabled us to continue investing aggressively in product development and to expand our employee team—adding 78 new employees over the course of the year.

> Tyler's deep domain expertise gives us an insider's insight into the unique needs of local governments. With this knowledge, we deliver highly responsive software solutions that evolve as the public sector does.

Free Cash Flow
(In Millions)



[a] *excludes capital expenditures for office facilities of $9.4 million in 2009 and $16.0 million in 2008.*

In addition to expanding our team, Tyler made significant investments in our existing software portfolio to develop new features and functionality. We also continued to invest in new products in the education market and in our Microsoft Dynamics AX development effort for the public sector that's slated for release in early 2011.

Tyler also made several small acquisitions that augment our offerings in specific product or geographic areas. To expand the geographic reach of our land and vital records business, we acquired Parker-Lowe & Associates in North Carolina, which develops software designed for registering and retrieving deeds for land records and social services offices. We also acquired Assessment Evaluation Services Inc., which develops integrated property appraisal solutions and applications unique to California.

Additionally, we acquired technology that delivers specialized information and data warehouse solutions for K–12 school and local government markets. In January 2010, Tyler completed the acquisition of Wiznet, which provides software products and services that simplify the electronic filing and management of documents related to court cases. Looking to the future, we will continue to seek opportunities to expand our product offerings and customer base through strategic acquisitions at reasonable valuations.

Delivering Greater Accessibility

From the nation's largest counties to the smallest rural agencies, Tyler Technologies understands that each of our clients deserves the best possible return on its technology investment—not to mention a high degree of flexibility. Delivering long-term scalability by providing regular product updates with new features and functionality is particularly important in the public sector because it's not uncommon for local governments and schools to keep their systems for much longer than organizations in the private sector.

As a result, many agencies are using a potpourri of software and hardware solutions that are no longer supported—because the vendor is no longer in business or simply hasn't invested in new technology. It can also pose challenges for governments when personnel with proprietary knowledge of these legacy systems retire or leave the organization.

Tyler's Software-as-a-Service (SaaS) model gives clients seamless access to the innovative software solutions they need. Through a subscription-based arrangement, Tyler hosts and manages both software and data. By opting for the SaaS model, our clients can avoid making capital investments to overhaul their infrastructure and can access these sophisticated systems with significantly fewer in-house resources.

Expanding Our Visibility

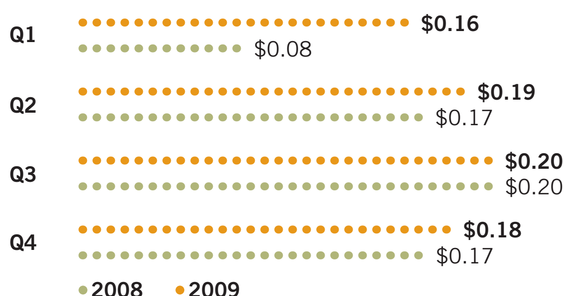
Over the years, one of our core strategies for growth has been to improve Tyler's visibility and expand sales in regions where our products previously had limited presence. By updating Tyler's brand identity and messaging, we now have a more cohesive platform to effectively market our products in new regions—as well as existing ones where we already have a presence.

Tyler continued adding new clients in key markets throughout 2009. For example, we secured a deal with Denver Public Schools for our transportation management system, a product we added to our portfolio in 2008. Tyler also introduced our financial management and citizen service solutions in five public sector agencies within California, and we secured a deal with the City of Nashville and Davidson County (Tennessee) for our courts & justice solutions.

Given the exceptional breadth and depth of our product portfolio, many of our existing clients turn to Tyler when the time comes to upgrade or add new software applications. This provides Tyler a prime opportunity to cross-sell our broad line of software solutions.

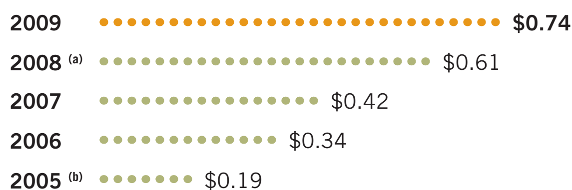
No matter how large or small, Tyler provides public sector organizations of all sizes access to a broad range of innovative software solutions that address their unique needs.

2008-2009 Quarterly EPS [a]
(In Dollars)



[a] *2008 EPS is non-GAAP and excludes non-cash legal settlement charge related to warrants of $0.16 in Q2, $0.04 in Q3 and $0.03 in Q4*

Diluted Annual EPS
(In Dollars)



[a] *2008 EPS is non-GAAP and excludes non-cash legal settlement charge related to warrants of $0.23*

[b] *includes restructuring charge of $0.02*

For example, we won a $2.5 million contract for our jail management and law enforcement solutions with Collin County, Texas, which has used Tyler's court case management solution since 2006. We also secured a number of deals with clients who purchased multiple Tyler solutions at the same time. Tyler also integrated our transportation management solution with our financial management solution for the Fort Worth (Texas) Independent School District to streamline invoicing, budgetary control, reconciliation, and account management.

Rita Lewis-Devereaux
Appraisal & Property Tax Solutions

Speaking from Passion. Rita Lewis-Devereaux is no stranger to anticipating needs when it comes to helping local governments effectively and efficiently appraise all types of properties. In fact, since 1973 she's been involved in the property tax field—including positions with Dekalb County, Georgia, as deputy tax commissioner, appraisal auditor and software project manager. Rita also served as vice chairman of the Board of Assessors for Fulton County (Atlanta), Georgia. Prior to joining the Tyler team as a lead business analyst in 2001, Rita had used Tyler's appraisal products for more than two decades. Today, she helps appraisal jurisdictions of all sizes implement Tyler's appraisal and property tax solutions. It's a role that suits her well, she says, not only because of her extensive understanding of the public sector and Tyler's solutions—but, more importantly, because she enjoys guiding clients through the implementation process. "I really love the creativity in what I do and helping clients bring the software live," Rita explains. "I couldn't ask for a better job—it's perfect for me."

Brock Taylor
Land & Vital Records Solutions

Speaking from Service. Far beyond the "Comments Welcome" box organizations once used, Brock Taylor, manager of the Land Records Office for Boulder County, Colorado, shared his wish list of software features directly with the source—Tyler. Beyond the software's ability to streamline Boulder County's Land Records Office, it was Tyler's client-centric approach that impressed Brock the most—and eventually is what led him to join Tyler. And for the past 12 years, Brock has been helping other land records offices streamline their operations as a product manager. "Understanding the client experience is invaluable," explains Brock. "I'm now able to reflect on how clients use the software and appreciate the reasons behind their development requests."

While Tyler has historically focused on serving the needs of small and mid-sized governments, in recent years we have gained a stronger foothold in larger, metropolitan markets. These markets are especially significant as they provide considerable revenue growth and margin expansion potential.

Tyler consistently expanded its presence in new geographic areas and secured larger deals in 2009—further solidifying our position as a market leader in public sector software.

Tyler secured a number of larger deals, including a $5.9 million contract with Hillsborough County, Florida, for Tyler's integrated case management software. We also signed a $2.2 million contract with San Antonio, Texas, the nation's seventh largest city, for our municipal court case management solution. In a deal valued at $3.5 million, Dakota County, Minnesota, the state's fourth largest county, purchased our appraisal and property tax software. The cities of Bridgeport, Connecticut, and Chesapeake, Virginia, will implement our financial management solution under contracts valued at approximately $2 million each.

Looking Ahead

Closing out 2009, Tyler delivered another solid year by consistently executing our growth strategies. Given our extensive experience in delivering proven software solutions and our growing presence in key markets, we look to carry this momentum into 2010 and beyond.

Tyler will continue to build upon the foundation we've established using our time-tested growth strategy of expanding into new geographic areas, enhancing our product offerings, cross-selling our solutions and securing larger deals. We believe we are well positioned for new growth, particularly with our Software-as-a-Service (SaaS) offerings.

Whether delivering the right types of solutions for local governments, providing an exceptional workplace for employees, or producing a solid return on investment for shareholders, Tyler Technologies speaks from experience. It is with this insight that we plan for the future. We empower those who serve the public. And we make a difference to the communities we serve.

Continuing the trend we've seen in recent years, many local governments—even those that had previously deployed Tyler software solutions on site—are now migrating to our SaaS model. Today, many of Tyler's products are available in a hosted format. Based on client response, including our near perfect retention rate, this model is proving to be incredibly effective and efficient at delivering clients greater flexibility and scalability. Although only comprising 6 percent of our total revenues in 2009, subscription revenues represented our fastest-growing revenue line, with an increase of 20 percent over 2008. Among the larger SaaS contracts we signed in 2009 were a $1.4 million deal with the City of Enfield, Connecticut, and a $1.2 million deal with Tualatin Valley (Oregon) Fire & Rescue.

Tyler Technologies' success in 2009 is a continuation of the strong foundation we've established in years past. Through careful planning, consistent execution and an unwavering commitment to our clients, Tyler has become the brand of choice for essential software solutions that can respond to the ever-changing needs of the public sector market. Building from our record-setting year in 2008, Tyler Technologies grew revenues, expanded gross and operating margins and increased earnings per share during 2009—even while aggressively investing in product development. The following financial statements detail our results.

Our common stock is traded on the New York Stock Exchange under the symbol "TYL." At December 31, 2009, we had approximately 2,115 stockholders of record. A number of our stockholders hold their shares in street name; therefore, there are substantially more than 2,115 beneficial owners of our common stock.

The following table shows, for the calendar periods indicated, the high and low sales price per share of our common stock as reported on the New York Stock Exchange.

		High	Low
2008:	First Quarter	$14.70	$12.29
	Second Quarter	15.97	13.33
	Third Quarter	18.47	13.29
	Fourth Quarter	15.17	9.79
2009:	First Quarter	$14.79	$11.35
	Second Quarter	17.76	14.17
	Third Quarter	17.62	14.51
	Fourth Quarter	21.09	16.76

We did not pay any cash dividends in 2009 or 2008. Our bank credit agreement contains restrictions on the payment of cash dividends. We intend to retain earnings for use in the operation and expansion of our business, and, therefore, we do not anticipate declaring a cash dividend in the foreseeable future.

During 2009, we purchased approximately $1.2 million shares of our common stock for an aggregate purchase price of $17.0 million. The repurchase program, which was approved by our board of directors, was announced in October 2002, and was amended in April and July 2003, October 2004, October 2005, May 2007, May 2008, October 2008 and May 2009. Our board of directors authorized the repurchase of an additional 2.0 million shares on May 14, 2009. As of December 31, 2009, we had remaining authorization to repurchase up to 2.3 million additional shares of our common stock. There is no expiration date specified for the authorization and we intend to repurchase stock under the plan from time to time. Our bank credit agreement contains restrictions on the amount of common stock we may purchase.

SELECTED FINANCIAL DATA

	For the Years Ended December 31,				
(In thousands, except per share data)	2009	2008	2007	2006	2005
STATEMENT OF OPERATIONS DATA:					
Revenues	$290,286	$265,101	$219,796	$195,303	$170,457
Costs and expenses:					
Cost of revenues [1]	161,523	155,314	135,371	120,499	108,970
Selling, general and administrative expenses [1]	70,115	62,923	51,724	48,389	43,821
Research and development expense	11,159	7,286	4,443	3,322	2,421
Restructuring charge	—	—	—	—	1,260
Amortization of customer and trade name intangibles	2,705	2,438	1,478	1,318	1,266
Non-cash legal settlement related to warrants [2]	—	9,045	—	—	—
Operating income	44,784	28,095	26,780	21,775	12,719
Other (expense) income, net	(146)	1,181	1,800	1,080	906
Income from operations before income taxes	44,638	29,276	28,580	22,855	13,625
Income tax provision	17,628	14,414	11,079	8,493	5,432
Net income	$ 27,010	$ 14,862	$ 17,501	$ 14,362	$ 8,193
Net income per diluted share	$ 0.74	$ 0.38	$ 0.42	$ 0.34	$ 0.19
Weighted average diluted shares	36,624	39,184	41,352	41,868	42,075
STATEMENT OF CASH FLOWS DATA:					
Cash flows provided by operating activities	$ 42,941	$ 47,802	$ 34,111	$ 26,804	$ 21,187
Cash flows (used by) provided by investing activities	(13,658)	(9,554)	(34,275)	(24,326)	1,820
Cash flows used by financing activities	(21,349)	(46,128)	(7,406)	(5,999)	(14,847)
BALANCE SHEET DATA:					
Total assets	$270,670	$251,761	$241,508	$220,276	$194,437
Shareholders' equity	134,358	114,262	137,211	125,875	112,197

(1) Effective January 1, 2006, we adopted the fair value recognition provisions of Accounting Standards Codification 718, Stock Compensation, using the modified-prospective method. In 2009, 2008, 2007 and 2006, respectively, cost of revenues included $540,000, $364,000, $227,000 and $147,000 share-based compensation expense. Selling, general and administrative expenses in 2009, 2008, 2007 and 2006, respectively, included $4.5 million, $3.5 million, $2.1 million and $1.8 million share-based compensation expense. In accordance with the standard, results of operations for the year 2005 are reported under the previous accounting standard and no expense was recorded.

(2) On June 27, 2008, we settled outstanding litigation related to two Stock Purchase Warrants (the "Warrants") owned by Bank of America, N. A. ("BANA"). The Warrants entitled BANA to acquire 1.6 million shares of Tyler common stock at an exercise price of $2.50 per share. Following court-ordered mediation, in July 2008, BANA paid us $2.0 million and we issued to BANA 801,883 restricted shares of Tyler common stock. Accordingly, we recorded a non-cash legal settlement related to warrants charge of $9.0 million, which was not tax deductible.

FORWARD-LOOKING STATEMENTS

In addition to historical information, this Annual Report contains forward-looking statements. The forward-looking statements are made in reliance upon safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those reflected in the forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's opinions only as of the date hereof. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements. Readers should carefully review the risk factors described in documents we file from time to time with the SEC.

When used in this Annual Report, the words "believes," "expects," "anticipates," "foresees," "forecasts," "estimates," "plans," "intends," "continues," "may," "will," "should," "projects," "might," "could" or the negative of such terms and similar expressions are intended to identify forward-looking statements. Similarly, statements that describe our business strategy, outlook, objectives, plans, intentions or goals also are forward-looking statements.

OVERVIEW

General

We provide integrated information management solutions and services for the public sector, with a focus on local governments. We develop and market a broad line of software products and services to address the information technology ("IT") needs of cities, counties, schools and other local government entities. In addition, we provide professional IT services to our customers, including software and hardware installation, data conversion, training and for certain customers, product modifications, along with continuing maintenance and support for customers using our systems. We also provide subscription-based services such as hosted solutions as well as property appraisal outsourcing services for taxing jurisdictions.

Our products generally automate three major functional areas:

- Financial Management and Education;
- Courts and Justice; and
- Property Appraisal and Tax and Other.

We monitor and analyze several key performance indicators in order to manage our business and evaluate our financial and operating performance. These indicators include the following:

- Revenues – We derive our revenues from five primary sources: sale of software licenses; subscription-based services; software services; maintenance and support; and appraisal services. Because the majority of the software we sell is "off-the-shelf," increased sales of software products generally result in incrementally higher gross margins. Thus, the most significant driver to our business is the number and size of software license sales. In addition, new software license sales generally generate implementation services revenues as well as future maintenance and support revenues, which are a recurring revenue source. We also monitor our customer base and churn since our maintenance and support revenue should increase due to our historically low customer turnover. During 2009, approximately 43% of our revenue was attributable to ongoing support and maintenance agreements and our customer turnover was approximately 2%.

- Cost of Revenues and Gross Margins – Our primary cost component is personnel expenses in connection with providing software implementation, subscription-based services, maintenance and support, and appraisal services to our customers. We can improve gross margins by controlling headcount and related costs and by expanding our revenue base, especially from those products and services that produce incremental revenue with minimal incremental cost, such as software licenses, subscription-based services, and maintenance and support. Our appraisal projects are seasonal in nature, and we often employ appraisal personnel on a short-term basis to coincide with the life of a project. As of December 31, 2009, our total employee count increased to 2,018 from 1,940 at December 31, 2008. Approximately a third of these additions were to our implementation and support staff, including additions that increased our capacity to deliver our backlog.

- Selling, General and Administrative ("SG&A") Expenses – The primary components of SG&A expense are administrative and sales personnel salaries and commissions, marketing expense, share-based compensation expense, rent and professional fees. Sales commissions generally fluctuate with revenues but other administrative expenses tend to grow at a slower rate than revenues.
- Liquidity and Cash Flows – The primary driver of our cash flows is net income. Uses of cash include acquisitions, capital investments in property and equipment and the discretionary purchases of treasury stock. In 2009, we purchased 1.2 million shares of our common stock for an aggregate purchase price of $17.0 million. We also paid $1.3 million for common stock repurchases accrued as of December 31, 2008. During 2009 we used cash of $2.9 million to acquire two companies and invested $12.4 million in property and equipment. Our investment in property and equipment included $9.4 million for an office building and we expect to pay the final retainage payment of $1.8 million for this office building by mid-2010. We also paid-down $8.0 million on our short-term revolving line of credit. Our working capital needs are fairly stable throughout the year with the significant components of cash outflows being payment of personnel expenses offset by cash inflows representing collection of accounts receivable and cash receipts from customers in advance of revenue being earned.
- Balance Sheet – Cash, accounts receivable and days sales outstanding and deferred revenue balances are important indicators of our business.

Acquisitions

On July 16, 2009, we completed the acquisition of certain assets of KPL, Inc. d/b/a Parker-Lowe & Associates ("Parker-Lowe") for $700,000 in cash. Parker-Lowe provides scanning and retrieval software and related services for land record and social services offices in local governments primarily in the North Carolina area. This acquisition was accounted for as a purchase of a business.

On April 3, 2009, we completed the acquisition of all of the capital stock of Assessment Evaluation Services, Inc. ("AES"). AES develops integrated property appraisal solutions and specializes in applications that deal with the unique provisions of the California Revenue and Taxation Code. The purchase price was approximately $1.1 million in cash.

In connection with these transactions we acquired total tangible assets of approximately $480,000 and assumed total liabilities of approximately $835,000, including $450,000 for contingent consideration for which we have paid $38,000 as of December 31, 2009. We recorded goodwill of approximately $1.3 million, all of which is expected to be deductible for tax purposes, and other intangible assets of approximately $820,000. The $820,000 of intangible assets is attributable to acquired software and customer relationships that will be amortized over a weighted average period of approximately 9 years. Our balance sheet as of December 31, 2009 reflects the allocation of the purchase price to the assets acquired and liabilities assumed based on their estimated fair values at the dates of acquisition.

The operating results of these acquisitions are included in our results of operations since the date of acquisition. We believe these acquisitions will complement our business by expanding our presence in certain geographic areas and adding to our customer base.

In the twelve months ended December 31, 2009, we also paid approximately $1.1 million for certain software assets to complement our tax and appraisal solutions and our student information management solutions.

Outlook

The financial market crisis has continued to disrupt credit and equity markets worldwide. Broad economic conditions remain uncertain and public sector entities continue to experience pressures that are reflected in longer than normal decision processes. Local and state governments may face financial pressures that could in turn affect our growth rate in the first quarter of 2010 and for the calendar year. While market conditions are not robust, we have great stability from the foundation of recurring revenues and high customer retention. Our base of recurring revenues from maintenance and support and subscription-based services is approximately 49% of total revenues. Consistent with our historical trends, we expect that first quarter 2010 earnings will not reach the level achieved in the fourth quarter of 2009 and will likely be below last year's first quarter earnings. We also expect that in excess of 60% of our annual earnings will occur in the second half of 2010.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of financial condition and results of operations is based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities at the date of the financial statements, the reported amounts of revenues, cost of revenues and expenses during the reporting period, and related disclosure of contingencies. The Notes to the Financial Statements included as part of this Annual Report describe our significant accounting policies used in the preparation of the financial statements. Significant items subject to such estimates and assumptions include the application of the percentage-of-completion and proportionate performance methods of revenue recognition, the carrying amount and estimated useful lives of intangible assets, determination of share-based compensation expense and valuation allowance for receivables. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies require significant judgments and estimates used in the preparation of our financial statements.

Revenue Recognition. We recognize revenues in accordance with the provisions of Accounting Standards Codification (" ASC") 605, Revenue Recognition and ASC 985-605, Software Revenue Recognition. Our revenues are derived from sales of software licenses, subscription-based services, appraisal services, maintenance and support, and services that typically range from installation, training and basic consulting to software modification and customization to meet specific customer needs. For multiple element software arrangements, which do not entail the performance of services that are considered essential to the functionality of the software, we generally record revenue when the delivered products or performed services result in a legally enforceable and non-refundable claim. We maintain allowances for doubtful accounts and sales adjustments, which are provided at the time the revenue is recognized. Because most of our customers are governmental entities, we rarely incur a loss resulting from the inability of a customer to make required payments. In a limited number of cases, we encounter a customer who is dissatisfied with some aspect of the software product or our service, and we may offer a "concession" to such customer. In those limited situations where we grant a concession, we rarely reduce the contract arrangement fee, but alternatively may perform additional services, such as additional training or programming a minor feature the customer had in their prior software solution. These amounts have historically been nominal. In connection with our customer contracts and the adequacy of related allowances and measures of progress towards contract completion, our project managers are charged with the responsibility to continually review the status of each customer on a specific contract basis. Also, we review, on at least a quarterly basis, significant past due accounts receivable and the adequacy of related reserves. Events or changes in circumstances that indicate that the carrying amount for the allowances for doubtful accounts and sales adjustments may require revision, include, but are not limited to, deterioration of a customer's financial condition, failure to manage our customer's expectations regarding the scope of the services to be delivered, and defects or errors in new versions or enhancements of our software products.

We use contract accounting, primarily the percentage-of-completion method, as discussed in ASC 605-35, Construction — Type and Certain Production — Type Contracts, for those software arrangements that involve significant production, modification or customization of the software, or where our software services are otherwise considered essential to the functionality of the software. We measure progress-to-completion primarily using labor hours incurred, or value added. In addition, we recognize revenue using the proportionate performance method of revenue recognition for our property appraisal projects, some of which can range up to five years. These methods rely on estimates of total expected contract revenue, billings and collections and expected contract costs, as well as measures of progress toward completion. We believe reasonably dependable estimates of revenue and costs and progress applicable to various stages of a contract can be made. At times, we perform additional and/or non-contractual services for little to no incremental fee to satisfy customer expectations. If changes occur in delivery, productivity or other factors used in developing our estimates of expected costs or revenues, we revise our cost and revenue estimates, and any revisions are charged to income in the period in which the facts that give rise to that revision first become known. In connection with these and certain other contracts, we may perform the work prior to when the services are billable and/or payable pursuant to the contract. The termination clauses in most of our contracts provide for the payment for the fair value of products delivered and services performed in the event of an early termination.

For subscription-based services such as application service provider arrangements and other hosting arrangements, we evaluate whether each of the elements in these arrangements represents a separate unit of accounting, as defined by ASC 605-25, Multiple Element Arrangements, using all applicable facts and circumstances, including whether (i) we sell or could readily sell the element unaccompanied by the other elements, (ii) the element has stand-alone value to the customer, (iii) there is objective reliable evidence of the fair value of the undelivered item, and (iv) there is a general right of return. We consider the applicability of ASC 605-55-121 and 122 with respect to arrangements that include the right to use software stored on another entity's hardware on a contract-by-contract basis. In hosted term-based agreements, where the customer does not have the contractual right to take possession of the software, hosting fees are recognized on a monthly basis over the term of the contract commencing when the customer has access to the software. For professional services associated with hosting arrangements that we determine do not have stand-alone value to the customer, we recognize the services revenue ratably over the remaining contractual period once hosting has gone live and we may begin billing for the hosting services. We record amounts that have been invoiced in accounts receivable and in deferred revenue or revenues, depending on whether the revenue recognition criteria have been met.

In connection with certain of our contracts, we have recorded retentions receivable or unbilled receivables consisting of costs and estimated profit in excess of billings as of the balance sheet date. Many of the contracts which give rise to unbilled receivables at a given balance sheet date are subject to billings in the subsequent accounting period. Management reviews unbilled receivables and related contract provisions to ensure we are justified in recognizing revenue prior to billing the customer and that we have objective evidence which allows us to recognize such revenue. In addition, we have a sizable amount of deferred revenue which represents billings in excess of revenue earned. The majority of this liability consists of maintenance billings for which payments are made in advance and the revenue is ratably earned over the maintenance period, generally one year. We also have deferred revenue for those contracts in which we receive a deposit and the conditions in which to record revenue for the service or product has not been met. On a periodic basis, we review by customer the detail components of our deferred revenue to ensure our accounting remains appropriate.

Intangible Assets and Goodwill. Our business acquisitions typically result in the creation of goodwill and other intangible asset balances, and these balances affect the amount and timing of future period amortization expense, as well as expense we could possibly incur as a result of an impairment charge. The cost of acquired companies is allocated to identifiable tangible and intangible assets based on estimated fair value, with the excess allocated to goodwill. Accordingly, we have a significant balance of acquisition date intangible assets, including software, customer related intangibles, trade name and goodwill. In addition, we capitalize software development costs incurred subsequent to the establishment of technological feasibility. These intangible assets are amortized over their estimated useful lives. All intangible assets with definite and indefinite lives are reviewed for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Recoverability of goodwill is generally measured by a comparison of the carrying amount of an asset to its fair value, generally determined by estimated future net cash flows expected to be generated by the asset. We evaluate goodwill for impairment annually as of April, or more frequently if impairment indicators arise. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. The fair values calculated in our impairment tests are determined using discounted cash flow models involving several assumptions. These assumptions include, but are not limited to, anticipated operating income growth rates, our long-term anticipated operating income growth rate and the discount rate. Our cash flow forecasts are based on assumptions that are consistent with the plans and estimates we are using to manage the underlying businesses. The assumptions that are used are based upon what we believe a hypothetical marketplace participant would use in estimating fair value. We have identified two reporting units for impairment testing. Our reporting units are the same as our reportable segments and consistent with the reporting units tested for impairment in prior years. Assets, liabilities and goodwill have been assigned to reporting units based on assets acquired and liabilities assumed as of the date of acquisition. We evaluate the reasonableness of the fair value calculations of our reporting units by comparing the total of the fair value of all of our reporting units to our total market capitalization. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain.

Recoverability of other intangible assets is generally measured by comparison of the carrying amount to estimated undiscounted future cash flows. The assessment of recoverability or of the estimated useful life for amortization purposes will be affected if the timing or the amount of estimated future operating cash flows is not achieved. Such indicators may include, among others: a significant decline in expected future cash flows; a sustained, significant decline in stock price and market capitalization; a significant adverse change in legal factors or in the business climate; unanticipated competition; and reductions in growth rates. In addition, products, capabilities, or technologies developed by others may render our software products obsolete or non-competitive. Any adverse change in these factors could have a significant impact on the recoverability of goodwill or other intangible assets.

Our annual goodwill impairment analysis, which we performed during the second quarter of 2009, did not result in an impairment charge. During 2009 we did not identify any triggering events which would require an update to our annual impairment. A hypothetical 10% decrease in the fair value of either of our reporting units as of December 31, 2009 would have had no impact on the carrying value of our goodwill.

Share-Based Compensation. We have a stock option plan that provides for the grant of stock options to key employees, directors and non-employee consultants. We estimate the fair value of share-based awards on the date of grant using the Black-Scholes option valuation model. Share-based compensation expense includes the estimated effects of forfeitures, which will be adjusted over the requisite service period to the extent actual forfeitures differ, or are expected to differ from such estimates. Changes in estimated forfeitures are recognized in the period of change and will also impact the amount of expense to be recognized in future periods. Forfeiture rate assumptions are derived from historical data. We estimate stock price volatility at the date of grant based on the historical volatility of our common stock. Estimated option life is determined using the "simplified method" in accordance with Staff Accounting Bulletin No. 110. Determining the appropriate fair-value model and calculating the fair value of share-based awards at the grant date requires considerable judgment, including estimating stock price volatility, expected option life and forfeiture rates.

ANALYSIS OF RESULTS OF OPERATIONS AND OTHER

The following discussion compares the historical results of operations on a basis consistent with GAAP for the years ended December 31, 2009, 2008 and 2007.

2009 Compared to 2008

Revenues

The following table sets forth a comparison of the key components of our revenues for the following years ended December 31:

					Change	
($ in thousands)	2009	% of Total	2008	% of Total	$	%
Software licenses	$ 42,131	15%	$ 41,490	16%	$ 641	2%
Subscriptions	17,181	6	14,374	5	2,807	20
Software services	80,405	28	74,997	28	5,408	7
Maintenance	124,512	43	107,458	41	17,054	16
Appraisal services	18,740	6	19,098	7	(358)	(2)
Hardware and other	7,317	2	7,684	3	(367)	(5)
Total revenues	$290,286	100%	$265,101	100%	$25,185	10%

Software licenses. Software license revenues consist of the following components for the following years ended December 31:

					Change	
($ in thousands)	2009	% of Total	2008	% of Total	$	%
Financial management and education	$ 25,708	61%	$ 29,124	70%	$ (3,416)	(12)%
Courts and justice	13,801	33	10,128	24	3,673	36
Appraisal and tax and other	2,622	6	2,238	6	384	17
Total software license revenues	$ 42,131	100%	$ 41,490	100%	$ 641	2%

In 2009 we signed 74 large new contracts with average software license fees of approximately $307,000, compared to 72 large new contracts signed in 2008 with average software license fees of approximately $311,000. We consider contracts with a license fee component of $100,000 or more to be large. Although a contract is signed in a particular year, the year in which the revenue is recognized may be different because we recognize revenue according to our revenue recognition policy as described in Note 1 in the Notes to Financial Statements.

Changes in software license revenues consist of the following components:

- Software license revenue related to our financial management and education solutions declined $3.4 million compared to the prior year. We acquired several student information and financial management solutions for K-12 schools from January through August 2008. Excluding the impact of these acquisitions software license revenue would have declined $4.3 million. The decline was due to several factors. In 2009 our sales cycle to negotiate and close contracts which have reached the request for proposal phase lengthened slightly mainly due to budgetary constraints related to declining economic conditions. As a result the purchasing processes for some of our customers have been extended to include more approval and documentation requirements. The software installation period for most of our financial management and education solutions is relatively short and delays in the timing of signing new contracts will impact our results in the short term. In addition, a few contracts have included requirements to construct interfaces to existing systems or other essential functionality which results in recognizing revenue over a longer period of time. While we expect to continue to experience longer than normal sales cycles in 2010 and continued weakness through mid-2010, we currently expect financial management and education solutions software license revenues for 2010 to be slightly higher than 2009.
- Software license revenue related to our courts and justice software solutions increased $3.7 million in 2009 compared to 2008. Both 2009 and 2008 included approximately $1.7 million of revenue from contracts which had been deferred in accordance with the terms of these contracts. Courts and justice software license revenues were higher in 2009 due to contract arrangements that included more software license revenue than in the comparable prior year periods, slight price increases and improved installation processes as our primary courts and justice solution matures. In addition approximately $1.0 million of the increase related to achieving certain milestones for several contracts. We do not expect similar large adjustments to courts and justice software solutions revenue in 2010 due to recognition of revenue previously deferred in accordance with contract language. Therefore we currently expect courts and justice software solutions software license revenue in 2010 to increase at a much slower rate compared to 2009.

Subscriptions. Subscription-based services revenue primarily consists of revenues derived from application service provider ("ASP") arrangements and other hosted service offerings, software subscriptions and disaster recovery services. ASP and other software subscription agreements are typically for periods of three to six years and automatically renew unless either party cancels the agreement. Disaster recovery and miscellaneous other hosted service agreements are typically renewable annually. New customers for ASP and other hosted service offerings as well as existing customers who converted to our ASP model provided the majority of the subscription revenue increase with the remaining increase due to slightly higher rates for disaster recovery services. In June 2008, as a result of changes in its technology organization, one customer terminated its ASP arrangement with us and elected, as provided in the ASP contract, to purchase the software instead. This contract contributed approximately $450,000 of subscription revenue in each of the first two quarters of 2008.

Software services. Changes in software services revenues consist of the following components:

- Software services revenue related to financial management and education solutions, which comprise approximately 60% of our software services revenue in the periods presented, increased 5% compared to 2008. We acquired several student information and financial management solutions for K-12 schools from January through August 2008. Excluding the impact of these acquisitions, software services revenue increased 3%, which was mainly due to additions to our implementation and support staff as well as leverage in the utilization of our implementation and support staff.
- Software services revenue related to courts and justice solutions comprise approximately 30% of our software services revenues in the periods presented and increased 21% compared to 2008. These increases reflect our increased capacity to deliver backlog following additions to our implementation and support staff and slightly higher rates on some arrangements. Also, increased contract volume in our municipal courts software solutions, primarily in Texas, generated higher related services revenue.

Maintenance. We provide maintenance and support services for our software products and third party software. Maintenance revenues increased 16% in 2009 compared to 2008. Maintenance and support services grew 14% in 2009, excluding the impact of acquisitions. This increase was due to growth in our installed customer base and slightly higher maintenance rates on most of our product lines.

Appraisal services. Appraisal services revenue declined 2% in 2009 compared to 2008. The appraisal services business is somewhat cyclical and driven in part by statutory revaluation cycles in various states. We substantially completed several large appraisal projects mid-2009. We began several new revaluation contracts late 2009 and as a result currently expect appraisal revenues to increase slightly in 2010.

Cost of Revenues and Gross Margins

The following table sets forth a comparison of the key components of our cost of revenues and those components stated as a percentage of related revenues for the following years ended December 31:

($ in thousands)	2009	% of Related Revenues	2008	% of Related Revenues	Change $	Change %
Software licenses	$ 5,440	13%	$ 9,224	22%	$(3,784)	(41)%
Acquired software	1,411	3	1,799	4	(388)	(22)
Software services, maintenance and subscriptions	137,199	62	126,247	64	10,952	9
Appraisal services	11,518	61	12,251	64	(733)	(6)
Hardware and other	5,955	81	5,793	75	162	3
Total cost of revenues	$161,523	56%	$155,314	59%	$ 6,209	4%

The following table sets forth a comparison of gross margin percentage by revenue type for the periods presented for the following years ended December 31:

Gross Margin Percentages	2009	2008	Change
Software licenses and acquired software	83.7%	73.4%	10.3%
Software services, maintenance and subscriptions	38.2	35.9	2.3
Appraisal services	38.5	35.9	2.6
Hardware and other	18.6	24.6	(6.0)
Overall gross margin	44.4%	41.4%	3.0%

Software license and acquired software. Amortization expense for capitalized development costs on certain software products comprised approximately 15% of our cost of software license revenues in 2009 compared to approximately 50% of our cost of software license in 2008. The remaining balance is made up of third party software costs. Once a product is released, we begin to amortize, over the estimated useful life of the product, any capitalized costs associated with its development. Amortization expense is determined on a product-by-product basis at an annual rate not less than straight-line basis over the product's estimated life, which is generally five years. Development costs consist mainly of personnel costs, such as salary and benefits paid to our developers, and rent for related office space.

Cost of acquired software includes amortization expense for software acquired through acquisitions. We completed several acquisitions in the period 2007 through 2009 and these costs are being amortized over a weighted average period of approximately 5 years. In late 2008 software associated with one significant acquisition completed in December 2003 became fully amortized.

In 2009, our software license gross margin percentage rose significantly compared to the prior year periods because several products became fully amortized in late 2008, as did software acquired related to a significant acquisition in December 2003. We did not capitalize any internal software development costs in 2009 or 2008.

Software services, maintenance and subscription-based services. Cost of software services, maintenance and subscriptions primarily consists of personnel costs related to installation of our software, conversion of customer data, training customer personnel and support activities and various other services such as ASP and disaster recovery. In 2009, the software services,

maintenance and subscriptions gross margin increased compared to the prior year partly because maintenance and various other services such as ASP and disaster recovery costs typically grow at a slower rate than related revenues due to leverage in the utilization of our support and maintenance staff and economies of scale. We have increased our implementation and support staff for both the financial management and education solutions and courts and justice solutions by 51employees since 2008 in order to expand our capacity to implement our contract backlog. This increase was offset somewhat by 24 fewer employees for appraisal and tax solutions. The software services, maintenance and subscription-based services gross margin also benefited from slightly higher rates for certain services.

Appraisal services. Our appraisal gross margin increased compared to 2008 as the result of cost savings and operational efficiencies experienced on an unusually complex project. A high proportion of the costs of appraisal services revenue are variable, as we often hire temporary employees to assist in appraisal projects whose term of employment generally ends with the projects' completion.

Our blended gross margin for 2009 was higher than 2008 due to lower amortization expense of software development costs described above. The gross margin also benefited from leverage in the utilization of our support and maintenance staff and economies of scale and slightly higher rates on certain services.

Selling, General and Administrative Expenses

Selling, general and administrative ("SG&A") expenses consist primarily of salaries, employee benefits, travel, share-based compensation expense, commissions and related overhead costs for administrative and sales and marketing employees as well as, professional fees, trade show activities, advertising costs and other marketing related costs. The following table sets forth a comparison of our SG&A expenses for the following years ended December 31:

					Change	
($ in thousands)	2009	% of Revenues	2008	% of Revenues	$	%
Selling, general and administrative expenses	$70,115	24%	$62,923	24%	$7,192	11%

The increase in SG&A expenses included higher share-based compensation expense, commission costs and marketing expenses. Marketing expenses in 2009 include costs associated with the launch of a new corporate branding initiative. Our SG&A employee count increased 4% from 2008.

Research and Development Expense

Research and development expenses consist primarily of salaries, employee benefits and related overhead costs associated with product development and enhancements and upgrades provided to existing customers under maintenance plans. The following table sets forth a comparison of our research and development expense for the following years ended December 31:

					Change	
($ in thousands)	2009	% of Revenues	2008	% of Revenues	$	%
Research and development expense	$11,159	4%	$7,286	3%	$3,873	53%

Research and development expense consist mainly of costs associated with the Microsoft Dynamics AX project, in addition to costs associated with other new product development efforts. We have increased our research and development staff by 72 employees since 2008. In January 2007, we entered into a Software Development and License Agreement, which provided for a strategic alliance with Microsoft Corporation ("Microsoft") to jointly develop core public sector functionality for Microsoft Dynamics AX to address the accounting needs of public sector organizations worldwide. In September 2007, Tyler and Microsoft signed an amendment to the Software Development and License Agreement, which grants Microsoft intellectual property rights in and to certain portions of the software code provided and developed by Tyler into Microsoft Dynamics AX products to be marketed and sold outside of the public sector in exchange for reimbursement payments to partially offset the research and development costs.

In 2009 and 2008, we offset our research and development expense by $3.5 million and $1.8 million, respectively, which were the amounts earned under the terms of our agreement with Microsoft. In September 2008, Tyler and Microsoft signed a

statement of work under the Amended Software Development and License Agreement for which we currently expect to recognize offsets to our research and development expense by approximately $850,000 each quarter through the end of 2010. In addition, in October 2009, the scope of the project was further expanded that will result in additional offsets to research and development expense, varying in amount from quarter to quarter, with the first payment to be invoiced on August 31, 2010 and invoiced quarterly through March 31, 2012 for a total of approximately $6.2 million. The actual amount and timing of future research and development costs and related reimbursements and whether they are capitalized or expensed may vary.

Non-Cash Legal Settlement Related to Warrants

On June 27, 2008, we settled outstanding litigation related to the Warrants owned by Bank of America, N. A. (" BANA"). As disclosed in prior SEC filings, the Warrants entitled BANA to acquire 1.6 million shares of Tyler common stock at an exercise price of $2.50 per share. Following court-ordered mediation, in July 2008, BANA paid us $2.0 million and we issued to BANA 801,883 restricted shares of Tyler common stock. Accordingly, we recorded a non-cash legal settlement related to warrants charge of $9.0 million, which was not tax deductible.

Amortization of Customer and Trade Name Intangibles

Acquisition intangibles are comprised of the excess of the purchase price over the fair value of net tangible assets acquired that is allocated to acquired software and customer and trade name intangibles. The remaining excess purchase price is allocated to goodwill that is not subject to amortization. Amortization expense related to acquired software is included with cost of revenues, while amortization expense of customer and trade name intangibles is recorded as other operating expense. The estimated useful lives of both customer and trade name intangibles are 5 to 25 years. The following table sets forth a comparison of amortization of customer and trade name intangibles for the following years ended December 31:

			Change	
($ in thousands)	2009	2008	$	%
Amortization of customer and trade name intangibles	$2,705	$2,438	$267	11%

In 2009 we completed several acquisitions and purchased certain software assets to complement our tax and appraisal solutions and our student information management solutions. These transactions increased amortizable customer and trade name intangibles by approximately $625,000. This amount will be amortized over approximately 10 years.

Estimated annual amortization expense relating to customer and trade name acquisition intangibles, excluding acquired software for which the amortization expense is recorded as cost of revenues, for the next five years is as follows (in thousands):

2010	$2,654
2011	2,638
2012	2,586
2013	2,427
2014	2,426

Other

Other (expense) income in 2009 and 2008 includes non-usage and other fees associated with a credit agreement entered into in October 2008. Other income in 2008 also included $1.1 million of interest income which declined due to significantly lower invested cash balances in 2009. Our invested cash balances declined due to purchases of treasury stock and investments in office facilities in late 2008 and 2009.

Income Tax Provision

The following table sets forth a comparison of our income tax provision for the following years ended December 31:

			Change	
($ in thousands)	2009	2008	$	%
Income tax provision	$17,628	$14,414	$3,214	22%
Effective income tax rate	39.5%	49.2%		

Our effective income tax rate declined compared to 2008 mainly due to a non-cash legal settlement related to warrants charge of $9.0 million in 2008, which was not deductible. In addition to the impact of the non-deductible non-cash legal settlement charge in 2008, the effective income tax rate for both years were different from the statutory United States federal income tax rate of 35% due to state income taxes, non-deductible share-based compensation expense, the qualified manufacturing activities deduction, and non-deductible meals and entertainment costs.

Approximately 40% of our stock option awards qualify as incentive stock options ("ISOs") for income tax purposes. As such, a tax benefit is not recorded at the time the compensation cost related to the options is recorded for book purposes due to the fact that an ISO does not ordinarily result in a tax benefit unless there is a disqualifying disposition. Non-qualified stock options result in the creation of a deferred tax asset, which is a temporary difference, until the time that the option is exercised. Due to the treatment of ISOs for tax purposes, our effective tax rate from year to year is subject to variability.

2008 Compared to 2007

Revenues

The following table sets forth a comparison of the key components of our revenues for the following years ended December 31:

					Change	
($ in thousands)	2008	% of Total	2007	% of Total	$	%
Software licenses	$ 41,490	16%	$ 35,063	16%	$ 6,427	18%
Subscriptions	14,374	5	10,406	5	3,968	38
Software services	74,997	28	60,283	27	14,714	24
Maintenance	107,458	41	85,411	39	22,047	26
Appraisal services	19,098	7	21,318	10	(2,220)	(10)
Hardware and other	7,684	3	7,315	3	369	5
Total revenues	$265,101	100%	$219,796	100%	$45,305	21%

Software licenses. Software license revenues consist of the following components for the following years ended December 31:

					Change	
($ in thousands)	2008	% of Total	2007	% of Total	$	%
Financial management and education	$29,124	70%	$ 27,236	78%	$ 1,888	7%
Courts and justice	10,128	24	5,987	17	4,141	69
Appraisal and tax and other	2,238	6	1,840	5	398	22
Total software license revenues	$41,490	100%	$ 35,063	100%	$ 6,427	18%

Changes in software license revenues consist of the following components:

- Software license revenue related to our financial management and education solutions for 2008 increased 7% compared to the prior year. Revenue from student information management solutions as well as student transportation management solutions acquired in the last twelve months contributed substantially to the increase. The remaining increase was mainly due to contract arrangements that included more software license revenue than in the past.
- Software license revenue related to our courts and justice software solutions increased 69% for 2008 compared to the prior year. New statewide contracts in Indiana and New Mexico contributed approximately two-thirds of the increase. The remaining increase was primarily due to an expanded presence in the markets for municipal courts software solutions and public safety software solutions.

Subscriptions. New ASP customers and existing customers converting to ASP arrangements provided the majority of the subscription revenue increase with the remaining increase due to new disaster recovery customers and slightly higher rates for disaster recovery services.

Software services. Changes in software services revenues consist of the following components:

- Software services revenue related to financial management and education solutions, which comprises slightly more than half of our software services revenue in the years presented, increased substantially compared to 2007. This increase was driven in part by increased capacity to deliver backlog following additions to our implementation and support staff since 2007 and due to larger and more complex contracts, which include more programming and project management services. In addition, we acquired a student transportation management solution in January 2008 which contributed approximately $3.9 million to software service revenues in 2008. Excluding the impact of acquisitions, we added approximately 95 employees to our financial management and education implementation and training staff during 2008.
- Software services revenue related to our courts and justice solutions experienced strong increases compared to 2007, reflecting increased capacity to deliver backlog following additions to our implementation and support staff since mid-2007. In addition, increased contract volume for municipal courts software solutions and public safety software solutions also generated higher related services revenue. We added approximately 12 employees to our courts and justice implementation and training staff during 2008.

Maintenance. Maintenance revenues increased 26% in 2008 compared to 2007. Excluding the impact of acquisitions, maintenance and support services grew 16% in 2008. This increase was due to growth in our installed customer base and slightly higher maintenance rates on most of our product lines.

Appraisal services. Appraisal services revenue declined 10% in 2008 compared to 2007. In late 2007, we substantially completed several projects related to the Ohio revaluation cycle, which occurs every six years, as well as a few other large contracts. Appraisal revenues for the first six months of 2008 were down 23% compared to the first six months of 2007. In mid-2008 we began a complete reappraisal of real property in Orleans Parish, Louisiana. As a result of this contract and an overall increase in contract volume, appraisal revenues for the last six months of 2008 increased 4% over the last six months of 2007.

Cost of Revenues and Gross Margins

The following table sets forth a comparison of the key components of our cost of revenues and those components stated as a percentage of related revenues for the following years ended December 31:

($ in thousands)	2008	% of Related Revenues	2007	% of Related Revenues	Change $	Change %
Software licenses	$ 9,224	22%	$ 7,953	23%	$ 1,271	16%
Acquired software	1,799	4	2,279	7	(480)	(21)
Software services, maintenance and subscriptions	126,247	64	104,993	67	21,254	20
Appraisal services	12,251	64	14,467	68	(2,216)	(15)
Hardware and other	5,793	75	5,679	78	114	2
Total cost of revenues	$155,314	59%	$135,371	62%	$19,943	15%

The following table sets forth a comparison of gross margin percentage by revenue type for the periods presented for the following years ended December 31:

Gross Margin Percentages	2008	2007	Change
Software licenses and acquired software	73.4%	70.8%	2.6%
Software services, maintenance and subscriptions	35.9	32.7	3.2
Appraisal services	35.9	32.1	3.8
Hardware and other	24.6	22.4	2.2
Overall gross margin	41.4%	38.4%	3.0%

Software license. In 2008, our software license gross margin percentage rose compared to the prior year mainly due to strong license fee revenue increases. Because approximately one-half of our cost of software license revenues in both periods is comprised of amortization of capitalized development costs, increased license fee revenues inherently result in higher gross margins.

Software services, maintenance and subscription-based services. In 2008, the software services, maintenance and subscriptions gross margin increased compared to the prior year partly because maintenance and various other services such as ASP and disaster recovery costs typically grow at a slower rate than related revenues due to leverage in the utilization of our support and maintenance staff and economies of scale. We increased our implementation and support staff by 215 employees during 2008 in order to expand our capacity to implement our contract backlog. This increase includes 102 employees related to acquisitions completed in 2008.

Appraisal services. Our appraisal gross margin for 2008 was higher than the prior year due to cost savings associated with a significant complex reappraisal project.

Our blended gross margin in 2008 was higher than the prior year in large part due to leverage in the utilization of our support and maintenance staff and economies of scale, with resulting increases in gross margin for each revenue category.

Selling, General and Administrative Expenses

The following table sets forth a comparison of our SG&A expenses for the following years ended December 31:

					Change	
($ in thousands)	2008	% of Revenues	2007	% of Revenues	$	%
Selling, general and administrative expenses	$62,923	24%	$51,724	24%	$11,199	22%

Excluding the impact of acquisitions, our SG&A employee count increased 9% during 2008.

Research and Development Expense

The following table sets forth a comparison of our research and development expense for the following years ended December 31:

					Change	
($ in thousands)	2008	% of Revenues	2007	% of Revenues	$	%
Research and development expense	$7,286	3%	$4,443	2%	$2,843	64%

Research and development expense consist mainly of costs associated with the Microsoft Dynamics AX project, in addition to costs associated with other new product development efforts. In 2008 and 2007, we offset our research and development expense by $1.8 million and $1.6 million, respectively, which were the amounts earned under the terms of our research and development agreement with Microsoft.

Non-Cash Legal Settlement Related to Warrants

On June 27, 2008, we settled outstanding litigation related to the Warrants owned by BANA. The Warrants entitled BANA to acquire 1.6 million shares of Tyler common stock at an exercise price of $2.50 per share. Following court-ordered mediation, in July 2008, BANA paid us $2.0 million and we issued to BANA 801,883 restricted shares of Tyler common stock. Accordingly, we recorded a non-cash legal settlement related to warrants charge of $9.0 million, which was not tax deductible.

Amortization of Customer and Trade Name Intangibles

The following table sets forth a comparison of amortization of customer and trade name intangibles for the following years ended December 31:

			Change	
($ in thousands)	2008	2007	$	%
Amortization of customer and trade name intangibles	$2,438	$1,478	$960	65%

In 2008, we completed three acquisitions, which increased amortizable customer and trade name intangibles by $12.3 million.

Other

Interest income was the main component of other income in both 2008 and 2007. Other income in 2008 also includes non-usage and other fees associated with a credit agreement entered into in October 2008. Interest income in 2008 was $1.1 million compared to $1.8 million in 2007. Interest income declined due to lower invested cash balances and slightly lower interest rates. Our invested cash balances declined due to purchases of treasury stock and investments in office facilities in 2008.

Income Tax Provision

The following table sets forth a comparison of our income tax provision for the following years ended December 31:

			Change	
($ in thousands)	2008	2007	$	%
Income tax provision	$14,414	$11,079	$3,335	30%
Effective income tax rate	49.2%	38.8%		

Our effective income tax rate increased approximately twelve points compared to the prior year due to a non-cash legal settlement related to warrants charge of $9.0 million, which was not deductible. The effective income tax rates were different from the statutory United States federal income tax rate of 35% primarily due to non-cash legal settlement related to warrants charge which was not deductible, as well as state income taxes, non-deductible share-based compensation expense, the qualified manufacturing activities deduction, and non-deductible meals and entertainment costs.

BUSINESS SEGMENT DISCUSSION

Enterprise Software Solutions

	2009	% Change	2008	% Change	2007
Revenue	$250,059	11%	$225,887	24%	$182,065
Gross margin	$114,309		$ 97,214		$ 71,684
Gross margin percentage	46%		43%		39%
Segment operating income	$ 55,639	17%	$ 47,698	37%	$ 34,833

In 2009 software license revenues were flat compared to 2008. Growth in recurring revenues from subscription-based services and maintenance experienced a 14% increase, excluding the impact of acquisitions, and was the primary factor for the increase in overall revenue and segment operating income for the Enterprise Software Solutions segment. This increase was due to growth in our installed customer base and slightly higher maintenance rates on most of our product lines. New customers for ASP and other hosted service offerings as well as existing customers converting to ASP arrangements and slightly higher rates for disaster recovery services also contributed to this increase. The gross margin and segment operating income rose in 2009 due to lower amortization expense of software development costs. The gross margin and segment operating income also benefited from leverage in the utilization of our support and maintenance staff and economies of scale and slightly higher rates on certain services.

In 2008 software license revenues were 18% higher than 2007 mainly due to higher courts and justice contract volume as a result of an expanded presence in Indiana and New Mexico. 2008 software license revenue also benefitted from student information management solutions and transportation solutions acquired in early 2008. Excluding the impact of acquisitions in 2008, revenues from subscription-based arrangements and maintenance grew by 19% compared to 2007 primarily due to growth in our customer base. Our gross margin and segment operating income in 2008 was higher than 2007 in large part due to leverage in the utilization of our support and maintenance staff and economies of scale and higher software license revenues.

Appraisal and Tax Software Solutions and Services

	2009	% Change	2008	% Change	2007
Revenue	$40,776	5%	$38,868	1%	$38,649
Gross margin	$15,489		$13,231		$12,966
Gross margin percentage	38%		34%		34%
Segment operating income	$ 6,949	28%	$ 5,448	8%	$ 5,040

In 2009 overall revenues for the Appraisal and Tax Software Solutions and Services segment increased compared to 2008 mainly due to a 16% increase in subscription-based arrangements and maintenance due to growth in our customer base and slightly higher rates. Excluding the results of acquisitions, subscription-based arrangements and maintenance increased 15% compared to 2008. This increase was offset slightly by 2% lower appraisal services. The appraisal services business is somewhat cyclical and driven in part by scheduled revaluation cycles in various states. We substantially completed several large appraisal projects mid-2009. Our appraisal gross margin and segment operating income increased compared to 2008 as the result of cost savings and operational efficiencies experienced on an unusually complex appraisal project. A high proportion of the costs of appraisal services revenue are variable, as we often hire temporary employees to assist in appraisal projects whose term of employment generally ends with the projects' completion.

Overall appraisal and tax revenues in 2008 were flat compared to 2007. Although maintenance revenues increased 8%, appraisal services revenues declined 10%. In late 2007, we substantially completed several appraisal projects related to the Ohio revaluation cycle, which occurs every six years, as well as a few other large contracts. The gross margin for 2008 was flat compared to 2007 due to cost savings associated with a significant complex reappraisal project which offset declines from lower contract volume.

FINANCIAL CONDITION AND LIQUIDITY

As of December 31, 2009, we had cash and cash equivalents (including restricted cash equivalents) of $15.7 million and current and non-current investments of $2.0 million, compared to cash and cash equivalents (including restricted cash equivalents) of $6.8 million and current and non-current investments of $4.6 million at December 31, 2008. As of December 31, 2009, we had no outstanding borrowings and outstanding letters of credit totaling $7.3 million to secure surety bonds required by some of our customer contracts. These letters of credit expire through mid-2010.

The following table sets forth a summary of cash flows for the years ended December 31:

($ in thousands)	2009	2008	2007
Cash flows provided by (used by):			
Operating activities	$ 42,941	$ 47,802	$ 34,111
Investing activities	(13,658)	(9,554)	(34,275)
Financing activities	(21,349)	(46,128)	(7,406)
Net increase (decrease) in cash and cash equivalents	$ 7,934	$ (7,880)	$ (7,570)

Net cash provided by operating activities continues to be our primary source of funds to finance operating needs and capital expenditures. Other capital resources include cash on hand, public and private issuances of debt and equity securities, and bank borrowings. The capital and credit markets have become more volatile and tightened as a result of adverse conditions that have caused the failure and near failure of a number of large financial services companies. It is possible that our ability to access the capital and credit markets may be limited by these or other factors. Notwithstanding the foregoing, we believe that cash provided by operating activities, cash on hand and our revolving credit agreement are sufficient to fund our working capital requirements, capital expenditures, income tax obligations, and share repurchases for the foreseeable future.

In 2009, operating activities provided net cash of $42.9 million, primarily generated from net income of $27.0 million, non-cash depreciation and amortization charges of $9.5 million, non-cash share-based compensation expense of $5.0 million and a decrease in working capital of $2.7 million offset slightly by a $1.7 million decrease related to deferred income taxes. Working capital declined due to higher accounts payable and accrued liabilities pertaining to timing of payments on vendor invoices and income tax liabilities and an accrued liability of $1.8 million for a retention payment related to construction of an office building. Other sources of working capital were deferred revenue related to December maintenance billings and a decrease in prepaid expenses. These working capital declines were offset somewhat by an increase in annual software maintenance billings as a result of growth in our installed customer base. The increase in accounts receivable was offset slightly by the collection of several large customer billings, one of which had been outstanding for over twelve months.

Cash flows provided by operating activities in 2008 included several advance payments from customers. In general, changes in the balance of deferred revenue are cyclical and primarily driven by the timing of our maintenance renewal billings. Our renewal dates occur throughout the year but our heaviest renewal cycles occur in the second and fourth quarters.

Non-current investments available-for-sale consist of two auction rate municipal securities ("ARS") which are collateralized debt obligations supported by municipal and state agencies and do not include mortgage-backed securities. Short-term investments available-for-sale consists of the portion of one of these ARS which was partially redeemed at par during the period January 1, 2010 through February 22, 2010. These ARS are debt instruments with stated maturities ranging from 22 to 33 years, for which the interest rate is designed to be reset through Dutch auctions approximately every 30 days. However, due to events in the credit markets, auctions for these securities have not occurred since February 2008. Both of our ARS have had very small partial redemptions at par in the period from July 2009 through February 2010. As of December 31, 2009 we have continued to earn and collect interest on both of our ARS. Because quoted prices in active markets are no longer available we determined the estimated fair values of these securities utilizing a discounted trinomial model. The model considers the probability of three potential occurrences for each auction event through the maturity date of each ARS. The three potential outcomes for each auction are (i) successful auction/early redemption, (ii) failed auction and (iii) issuer default. Inputs in determining the probabilities of the potential outcomes include but are not limited to, the securities' collateral, credit rating, insurance, issuer's financial standing, contractual restrictions on disposition and the liquidity in the market. The fair value of each ARS is determined by summing the present value of the probability-weighted future principal and interest payments determined by the model. Since there can be no assurances that auctions for these securities will be successful in the near future, we have classified our ARS as non-current investments.

In association with this estimate of fair value, we have recorded an after-tax temporary unrealized loss on our non-current ARS of $18,000, net of related tax effects of $10,000 in 2009, which is included in accumulated other comprehensive loss on our balance sheet. The unrealized loss includes the impact of adjusting previously recorded unrealized losses of approximately $120,000, net of related tax effects of $65,000 as of December 31, 2008 for several ARS which were subsequently redeemed for $2.5 million at par during 2009.

We consider the impairment in our ARS as temporary because we do not have the intent to sell, nor is it more-likely-than-not that we will be required to sell these securities before recovery of their cost basis. We believe that this temporary decline in fair value is due entirely to liquidity issues, because the underlying assets of these securities are supported by municipal and state agencies and do not include mortgage-backed securities, have redemption features which call for redemption at 100% of par value and have a current credit rating of A or AAA. The ratings on the ARS take into account credit support through insurance policies guaranteeing each of the bonds' payment of principal and accrued interest, if it becomes necessary. In addition, both ARS have had very small partial redemptions at par in the period July 2009 through February 2010. Based on our cash and cash equivalents balance of $15.7 million and expected operating cash flows, we do not believe a lack of liquidity associated with our ARS will adversely affect our ability to conduct business, and believe we have the ability to hold the securities throughout the currently estimated recovery period. We will continue to evaluate any changes in the market value of our ARS and in the future, depending upon existing market conditions, we may be required to record an other-than-temporary decline in market value.

At December 31, 2009, our days sales outstanding ("DSOs") were 98 days compared to DSOs of 99 days at December 31, 2008. DSOs are calculated based on accounts receivable (excluding long-term receivables, but including unbilled receivables) divided by the quotient of annualized quarterly revenues divided by 360 days.

Investing activities used cash of $13.7 million in 2009 compared to $9.6 million in 2008. In connection with plans to consolidate our workforce and support planned long-term growth, we paid $9.4 million for construction of an office building and expect to pay the final retainage of $1.8 million by mid-2010. We also liquidated $2.5 million of investments in ARS for cash at par. In 2009 we completed the acquisition of all of the capital stock of Assessment Evaluation Services, Inc. for $1.1 million in cash, paid $700,000 in cash for certain assets of KPL, Inc. d/b/a Parker-Lowe & Associates and acquired various software assets for $1.1 million in cash. Capital expenditures and acquisitions were funded from cash generated from operations.

In 2008, we liquidated $36.4 million of ARS investments for cash at par, and we completed the acquisitions of School Information Systems, Inc., VersaTrans Solutions Inc. and certain assets of Olympia Computing Company, Inc. d/b/a Schoolmaster to expand our presence in the education market. The combined purchase price, excluding cash acquired and including transaction costs, was approximately $23.9 million in cash and approximately 196,000 shares of Tyler common stock valued at $2.9 million. We paid $3.3 million, which included $2.1 million for land, for an office development. We also paid $12.7 million for an office building, land, and a related tenant lease in Yarmouth, Maine.

Cash used in financing activities was primarily comprised of purchases of treasury shares, net of proceeds from stock option exercises, payments on our revolving credit line and contributions from our employee stock purchase plan. During 2009, we purchased 1.2 million shares of our common stock for an aggregate purchase price of $17.0 million. We also paid $1.3 million for common stock repurchases accrued as of December 31, 2008.

The repurchase program, which was approved by our board of directors, was announced in October 2002, and was amended in April and July 2003, October 2004, October 2005, May 2007, May 2008, October 2008 and May 2009. Our board of directors authorized the repurchase of an additional 2.0 million shares on May14, 2009. As of December 31, 2009, we had remaining authorization to repurchase up to 2.3 million additional shares of our common stock. Our share repurchase program allows us to repurchase shares at our discretion and market conditions influence the timing of the buybacks and the number of shares repurchased. These share repurchases are funded using our existing cash balances as well as borrowings under our revolving credit agreement and may occur through open market purchase and transactions structured through investment banking institutions, privately negotiated transactions and/or other mechanisms. There is no expiration date specified for the authorization and we intend to repurchase stock under the plan from time to time. Our bank credit agreement contains restrictions on the amount of common stock we may purchase.

During 2008, we purchased 4.3 million shares of our common stock for an aggregate purchase price of $59.0 million.

In 2009 we issued 425,000 shares of common stock and received $2.3 million in aggregate proceeds upon exercise of stock options. In 2008 we received $1.8 million from the exercise of options to purchase approximately 379,000 shares of our common stock under our employee stock option plan and during 2007, we received $3.6 million from the exercise of options to purchase approximately 878,000 shares of our common stock under our employee stock option plan. In 2009 we received $1.5 million from contributions to the Tyler Technologies, Inc. Employee Stock Purchase Plan ("ESPP"). In both 2008 and 2007, we received $1.2 million from contributions to the ESPP.

Subsequent to December 31, 2009 and through February 22, 2010 we purchased approximately 59,000 shares of our common stock for an aggregate cash purchase price of $1.1 million.

In October 2008, we entered into a revolving bank credit agreement (the "Credit Facility") and a related pledge and security agreement which originally matured October 19, 2009. We amended and extended the related pledge and security agreement in October 2009. The Credit Facility matures October 18, 2010 and provides for total borrowings of up to $25.0 million and a $10.0 million Letter of Credit facility which can either be cash collateralized or issued using availability under the Credit Facility. The Credit Facility is secured by substantially all of our property. The Credit Facility requires us to maintain certain financial ratios and other financial conditions and prohibits us from making certain investments, advances, cash dividends or loans, restricts the amount of our common stock we may purchase and limits incurrence of additional indebtedness and liens. As of December 31, 2009, we were in compliance with those covenants. We expect borrowings to fund discretionary purchases of our common stock or fund acquisitions.

As of December 31, 2009, we had no outstanding borrowings and unused available borrowing capacity of $23.7 million under the Credit Facility. In addition, as of December 31, 2009, our bank had issued outstanding letters of credit totaling $7.3 million to secure surety bonds required by some of our customer contracts. These letters of credit have been collateralized by restricted cash balances of $6.0 million and $1.3 million of our available borrowing capacity and expire through mid-2010.

We paid income taxes, net of refunds received, of $18.1 million in 2009, $15.7 million in 2008, and $8.7 million in 2007.

In the first quarter of 2010 we acquired all the assets of Wiznet, Inc. ("Wiznet") for a cash purchase price of $9.5 million. Wiznet provides electronic document filing solutions for courts and law offices throughout the United States and is currently integrated with our primary courts and justice solution. We have not finalized the allocation of the purchase price.

Excluding acquisitions and final retainage payment of $1.8 million for an office building, we anticipate that 2010 capital spending will be between $3.7 million and $4.2 million. We expect the majority of our capital spending in 2010 will consist of computer equipment and software for infrastructure expansion. We currently do not expect to capitalize significant amounts related to software development in 2010, but the actual amount and timing of those costs, and whether they are capitalized or expensed may result in additional capitalized software development. Capital spending in 2010 is expected to be funded from existing cash balances and cash flows from operations.

From time to time we engage in discussions with potential acquisition candidates. In order to pursue such opportunities, which could require significant commitments of capital, we may be required to incur debt or to issue additional potentially dilutive securities in the future. No assurance can be given as to our future acquisition opportunities and how such opportunities will be financed.

We lease office facilities, as well as transportation, computer and other equipment used in our operations under non-cancelable operating lease agreements expiring at various dates through 2014. Most leases contain renewal options and some contain purchase options. Following are the future obligations under non-cancelable leases at December 31, 2009 (in thousands):

	2010	2011	2012	2013	2014	Thereafter	Total
Future rental payments under operating leases	$6,033	$5,265	$3,954	$2,365	$1,721	$ —	$19,338

As of December 31, 2009, we do not have any off-balance sheet arrangements, guarantees to third parties or material purchase commitments, except for the operating lease commitments listed above.

CAPITALIZATION

At December 31, 2009, our capitalization consisted of $134.4 million of shareholders' equity.

NEW ACCOUNTING PRONOUNCEMENTS

In September 2009, the Financial Accounting Standards Board issued ASU 2009-13, Multiple Element Arrangements. ASU 2009-13 addresses the determination of when the individual deliverables included in a multiple arrangement may be treated as separate units of accounting. ASU 2009-13 also modifies the manner in which the transaction consideration is allocated across separately identified deliverables and establishes definitions for determining fair value of elements in an arrangement. This new update is effective for fiscal years beginning on or after June 15, 2010. Early adoption is allowed. The new standard may impact our application service provider arrangements to recognize revenues, such as installation and data conversion, which are generally provided at the beginning of the arrangement as incurred instead of ratably over the life of the initial hosting term. The adoption of this standard is not expected to have a material impact on our financial condition or results of operation.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk represents the risk of loss that may affect us due to adverse changes in financial market prices and interest rates. Our investments available-for-sale consist of auction rate municipal securities ("ARS") which are collateralized debt obligations supported by municipal and state agencies and do not include mortgage-backed securities.

Non-current investments available-for-sale consist of two ARS with stated maturities ranging from 22 to 33 years, for which the interest rate is designed to be reset through Dutch auctions approximately every 30 days which would have qualified as Level 1 under ASC 820, Fair Value Measurements. However, due to events in the credit markets, auctions for these securities have not occurred since February 2008. Therefore, quoted prices in active markets are no longer available and we determined the estimated fair values of these securities as of December 31, 2009, utilizing a discounted trinomial model.

In association with this estimate of fair value, we have recorded an after-tax temporary unrealized loss on our non-current ARS of $18,000, net of related tax effects of $10,000 in 2009, which is included in accumulated other comprehensive loss on our balance sheet. The unrealized loss includes the impact of adjusting previously recorded unrealized losses of approximately $120,000, net of related tax effects of $65,000 as of December 31, 2008 for several ARS which were subsequently redeemed for $2.5 million at par during 2009. We consider the impairment in our ARS as temporary because we do not have the intent to sell, nor is it more-likely-than-not that we will be required to sell these securities before recovery of their cost basis. We believe that this temporary decline in fair value is due entirely to liquidity issues, because the underlying assets of these securities are supported by municipal and state agencies and do not include mortgage-backed securities, have redemption features which call for redemption at 100% of par value and have a current credit rating of A or AAA. The ratings on the ARS take into account credit support through insurance policies guaranteeing each of the bonds' payment of principal and accrued interest, if it becomes necessary. In addition, both ARS have had very small partial redemptions at par in the period July 2009 through February 2010. Based on our cash and cash equivalents balance of $15.7 million and expected operating cash flows, we do not believe a lack of liquidity associated with our ARS will adversely affect our ability to conduct business, and believe we have the ability to hold the securities throughout the currently estimated recovery period. We will continue to evaluate any changes in the market value of our ARS and in the future, depending upon existing market conditions, we may be required to record an other-than-temporary decline in market value.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Evaluation of Disclosure Controls and Procedures – We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act) designed to provide reasonable assurance that the information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. These include controls and procedures designed to ensure that this information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosures. Management, with the participation of the chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2009. Based on this evaluation the chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were effective as of December 31, 2009.

Management's Report on Internal Control Over Financial Reporting – Tyler's management is responsible for establishing and maintaining effective internal control over financial reporting as defined in Securities Exchange Act Rule 13a-15(f). Tyler's internal control over financial reporting is designed to provide reasonable assurance to Tyler's management and board of directors regarding the preparation and fair presentation of published financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Management assessed the effectiveness of Tyler's internal control over financial reporting as of December 31, 2009. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control—Integrated Framework.* Based on our assessment, we concluded that, as of December 31, 2009, Tyler's internal control over financial reporting was effective based on those criteria.

Tyler's internal control over financial reporting as of December 31, 2009 has been audited by Ernst & Young LLP, the independent registered public accounting firm who also audited Tyler's financial statements. Ernst & Young's attestation report on Tyler's internal control over financial reporting appears on page 38 hereof.

Changes in Internal Control Over Financial Reporting – During the quarter ended December 31, 2009, there were no changes in our internal control over financial reporting, as defined in Securities Exchange Act Rule 13a-15(f), that are materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Tyler Technologies, Inc.

We have audited Tyler Technologies, Inc.'s internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Tyler Technologies, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "Managements' Report on Internal Control Over Financial Reporting." Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

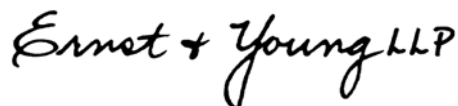
We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Tyler Technologies, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of Tyler Technologies, Inc. as of December 31, 2009 and 2008, and the related statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2009 and our report dated February 25, 2010 expressed an unqualified opinion thereon.



Dallas, Texas
February 25, 2010

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Tyler Technologies, Inc.

We have audited the accompanying balance sheets of Tyler Technologies, Inc. as of December 31, 2009 and 2008, and the related statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Tyler Technologies, Inc. at December 31, 2009 and 2008, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2009, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Tyler Technologies, Inc.'s internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 25, 2010 expressed an unqualified opinion thereon.

Dallas, Texas
February 25, 2010

STATEMENTS OF OPERATIONS

For the years ended December 31	2009	2008	2007
In thousands, except per share amounts			
Revenues:			
Software licenses	$ 42,131	$ 41,490	$ 35,063
Subscriptions	17,181	14,374	10,406
Software services	80,405	74,997	60,283
Maintenance	124,512	107,458	85,411
Appraisal services	18,740	19,098	21,318
Hardware and other	7,317	7,684	7,315
Total revenues	290,286	265,101	219,796
Cost of revenues:			
Software licenses	5,440	9,224	7,953
Acquired software	1,411	1,799	2,279
Software services, maintenance and subscriptions	137,199	126,247	104,993
Appraisal services	11,518	12,251	14,467
Hardware and other	5,955	5,793	5,679
Total cost of revenues	161,523	155,314	135,371
Gross profit	128,763	109,787	84,425
Selling, general and administrative expenses	70,115	62,923	51,724
Research and development expense	11,159	7,286	4,443
Amortization of customer and trade name intangibles	2,705	2,438	1,478
Non-cash legal settlement related to warrants	—	9,045	—
Operating income	44,784	28,095	26,780
Other (expense) income, net	(146)	1,181	1,800
Income before income taxes	44,638	29,276	28,580
Income tax provision	17,628	14,414	11,079
Net income	$ 27,010	$ 14,862	$ 17,501
Earnings per common share:			
Basic	$ 0.77	$ 0.39	$ 0.45
Diluted	$ 0.74	$ 0.38	$ 0.42
Basic weighted average common shares outstanding	35,240	37,714	38,735
Diluted weighted average common shares outstanding	36,624	39,184	41,352

See accompanying notes.

BALANCE SHEETS

December 31	2009	2008
In thousands, except share and per share amounts		
ASSETS		
Current assets:		
Cash and cash equivalents	$ 9,696	$ 1,762
Restricted cash equivalents	6,000	5,082
Short-term investments available-for-sale	50	775
Accounts receivable (less allowance for losses of $2,389 in 2009 and $2,115 in 2008)	81,245	76,989
Prepaid expenses	7,921	8,602
Other current assets	1,437	1,444
Deferred income taxes	3,338	2,570
Total current assets	109,687	97,224
Accounts receivable, long-term portion	1,018	197
Property and equipment, net	35,750	26,522
Non-current investments available-for-sale	1,976	3,779
Other assets:		
Goodwill	90,258	88,791
Customer related intangibles, net	25,490	27,438
Software, net	4,218	5,112
Trade name, net	2,063	2,471
Sundry	210	227
	$270,670	$251,761
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 3,807	$ 2,617
Accrued liabilities	26,110	22,913
Short-term revolving line of credit	—	8,000
Deferred revenue	99,116	95,773
Income taxes payable	220	166
Total current liabilities	129,253	129,469
Deferred income taxes	7,059	8,030
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, $10.00 par value; 1,000,000 shares authorized, none issued	—	—
Common stock, $0.01 par value; 100,000,000 shares authorized; 48,147,969 shares issued in 2009 and 2008	481	481
Additional paid-in capital	153,734	151,245
Accumulated other comprehensive loss, net of tax	(405)	(387)
Retained earnings	77,504	50,494
Treasury stock, at cost; 13,027,838 and 12,333,549 shares in 2009 and 2008, respectively	(96,956)	(87,571)
Total shareholders' equity	134,358	114,262
	$270,670	$251,761

See accompanying notes.

STATEMENTS OF SHAREHOLDERS' EQUITY

For the years ended December 31, 2009, 2008 and 2007

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock		Total Shareholders' Equity
In thousands	Shares	Amount				Shares	Amount	
Balance at December 31, 2006	48,148	$481	$151,627	$ (10)	$18,131	(9,256)	$(44,354)	$125,875
Comprehensive income:								
Net income	—	—	—	—	17,501	—	—	17,501
Unrealized gain on investment securities, net of tax	—	—	—	10	—	—	—	10
Total comprehensive income								17,511
Issuance of shares pursuant to stock compensation plan	—	—	(7,339)	—	—	878	10,928	3,589
Stock compensation	—	—	2,365	—	—	—	—	2,365
Treasury stock purchases	—	—	—	—	—	(1,250)	(16,163)	(16,163)
Issuance of shares pursuant to Employee Stock Purchase Plan	—	—	(2)	—	—	100	1,119	1,117
Federal income tax benefit related to exercise of stock options	—	—	2,917	—	—	—	—	2,917
Balance at December 31, 2007	48,148	481	149,568	—	35,632	(9,528)	(48,470)	137,211
Comprehensive income:								
Net income	—	—	—	—	14,862	—	—	14,862
Unrealized loss on investment securities, net of tax	—	—	—	(387)	—	—	—	(387)
Total comprehensive income								14,475
Issuance of shares pursuant to stock compensation plan	—	—	(3,495)	—	—	379	5,310	1,815
Stock compensation	—	—	3,820	—	—	—	—	3,820
Treasury stock purchases	—	—	—	—	—	(4,283)	(58,984)	(58,984)
Issuance of shares pursuant to Employee Stock Purchase Plan	—	—	(186)	—	—	101	1,376	1,190
Federal income tax benefit related to exercise of stock options	—	—	822	—	—	—	—	822
Issuance of shares in connection with legal settlement	—	—	455	—	—	802	10,595	11,050
Issuance of shares for acquisitions	—	—	261	—	—	196	2,602	2,863
Balance at December 31, 2008	48,148	481	151,245	(387)	50,494	(12,333)	(87,571)	114,262
Comprehensive income:								
Net income	—	—	—	—	27,010	—	—	27,010
Unrealized loss on investment securities, net of tax	—	—	—	(18)	—	—	—	(18)
Total comprehensive income								26,992
Issuance of shares pursuant to stock compensation plan	—	—	(3,774)	—	—	425	6,069	2,295
Stock compensation	—	—	5,045	—	—	—	—	5,045
Treasury stock purchases	—	—	—	—	—	(1,235)	(17,000)	(17,000)
Issuance of shares pursuant to Employee Stock Purchase Plan	—	—	(118)	—	—	115	1,546	1,428
Federal income tax benefit related to exercise of stock options	—	—	1,336	—	—	—	—	1,336
Balance at December 31, 2009	48,148	$481	$153,734	$(405)	$77,504	(13,028)	$(96,956)	$134,358

See accompanying notes.

STATEMENTS OF CASH FLOWS

For the years ended December 31	2009	2008	2007
In thousands			
Cash flows from operating activities:			
Net income	$ 27,010	$ 14,862	$ 17,501
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	9,497	12,611	11,211
Non-cash legal settlement related to warrants	—	9,045	—
Share-based compensation expense	5,045	3,820	2,365
Provision for losses – accounts receivable	1,538	1,764	753
Excess tax benefit from exercises of share-based arrangements	(1,125)	(666)	(1,891)
Deferred income tax benefit	(1,730)	(2,151)	(1,598)
Changes in operating assets and liabilities, exclusive of effects of acquired companies:			
Accounts receivable	(6,277)	(11,853)	(1,575)
Income tax payable	1,391	827	3,919
Prepaid expenses and other current assets	1,377	(338)	(304)
Accounts payable	1,190	(870)	(1,955)
Accrued liabilities	1,960	3,420	(1,619)
Deferred revenue	3,065	17,331	7,304
Net cash provided by operating activities	42,941	47,802	34,111
Cash flows from investing activities:			
Proceeds from sales of investments	2,500	45,065	45,480
Purchases of investments	—	(8,625)	(67,545)
Cost of acquisitions, net of cash acquired	(2,934)	(23,868)	(9,005)
Additions to property and equipment	(12,352)	(20,143)	(3,678)
Investment in software development costs	—	—	(167)
Acquired lease	—	(1,387)	—
(Increase) decrease in restricted investments	(918)	(620)	500
Decrease in other	46	24	140
Net cash used by investing activities	(13,658)	(9,554)	(34,275)
Cash flows from financing activities:			
(Decrease) increase in net borrowings on revolving credit facility	(8,000)	8,000	—
Purchase of treasury shares	(18,263)	(59,847)	(14,037)
Contributions from employee stock purchase plan	1,494	1,233	1,151
Proceeds from exercise of stock options	2,295	1,815	3,589
Excess tax benefits from exercise of share-based arrangements	1,125	666	1,891
Warrant exercise in connection with legal settlement	—	2,005	—
Net cash used by financing activities	(21,349)	(46,128)	(7,406)
Net increase (decrease) in cash and cash equivalents	7,934	(7,880)	(7,570)
Cash and cash equivalents at beginning of year	1,762	9,642	17,212
Cash and cash equivalents at end of year	$ 9,696	$ 1,762	$ 9,642

See accompanying notes.

(Tables in thousands, except per share data)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

DESCRIPTION OF BUSINESS

We provide integrated software systems and related services for the public sector, with a focus on local governments. We develop and market a broad line of software solutions and services to address the information technology ("IT") needs of cities, counties, schools and other local government entities. In addition, we provide professional IT services, including software and hardware installation, data conversion, training, and for certain customers, product modifications, along with continuing maintenance and support for customers using our systems. We also provide subscription-based services such as application service provider arrangements and other hosting services as well as property appraisal outsourcing services for taxing jurisdictions.

CASH AND CASH EQUIVALENTS

Cash in excess of that necessary for operating requirements is invested in short-term, highly liquid, income-producing investments. Investments with original maturities of three months or less are classified as cash and cash equivalents, which primarily consist of money market funds. Cash and cash equivalents are stated at cost, which approximates market value.

As of December 31, 2009, we had issued outstanding letters of credit totaling $7.3 million in connection with our surety bond program. These letters of credit have been collateralized by restricted cash balances of $6.0 million and $1.3 million of our available borrowing capacity. We do not believe these letters of credit will be required to be drawn upon. The letters of credit expire through mid-2010.

INVESTMENTS

Investments consist of auction rate municipal securities. These investments are classified as available-for-sale securities and are stated at fair value in accordance with Accounting Standards Codification ("ASC") 820, Fair Value Measurements and Disclosures. Unrealized holding gains and losses, net of the related tax effect, if any, are not reflected in earnings but are reported as a separate component of other comprehensive income until realized. The cost basis of securities sold is the specific cost of the auction rate municipal security. We account for the transactions as "Proceeds from sales of investments" for the security relinquished, and a "Purchases of investments" for the security purchased, in the accompanying Statements of Cash Flows.

REVENUE RECOGNITION

Software Arrangements:

We earn revenue from software licenses, subscriptions, software services, post-contract customer support ("PCS" or "maintenance"), and hardware. PCS includes telephone support, bug fixes, and rights to upgrades on a when-and-if available basis. We provide services that range from installation, training, and basic consulting to software modification and customization to meet specific customer needs. In software arrangements that include rights to multiple software products, specified upgrades, PCS, and/or other services, we allocate the total arrangement fee among each deliverable based on the relative fair value of each.

We typically enter into multiple element arrangements, which include software licenses, software services, PCS and occasionally hardware. The majority of our software arrangements are multiple element arrangements, but for those arrangements that involve significant production, modification or customization of the software, or where software services are otherwise considered essential to the functionality of the software in the customer's environment, we use contract accounting and apply the provisions of the Construction — Type and Production — Type Contracts as discussed in ASC 605-35.

If the arrangement does not require significant production, modification or customization or where the software services are not considered essential to the functionality of the software, revenue is recognized when all of the following conditions are met:

i. persuasive evidence of an arrangement exists;
ii. delivery has occurred;
iii. our fee is fixed or determinable; and
iv. collectability is probable.

For multiple element arrangements, each element of the arrangement is analyzed and we allocate a portion of the total arrangement fee to the elements based on the fair value of the element using vendor-specific objective evidence of fair value ("VSOE"), regardless of any separate prices stated within the contract for each element. Fair value is considered the price a customer would be required to pay if the element was sold separately based on our historical experience of stand-alone sales of these elements to third parties. For PCS, we use renewal rates for continued support arrangements to determine fair value. For software services, we use the fair value we charge our customers when those services are sold separately. We monitor our transactions to insure we maintain and periodically revise VSOE to reflect fair value. In software arrangements in which we have the fair value of all undelivered elements but not of a delivered element, we apply the "residual method", in compliance with ASC 985-605, Software Revenue Recognition, in accounting for any element of a multiple element arrangement involving software that remains undelivered such that any discount inherent in a contract is allocated to the delivered element. Under the residual method, if the fair value of all undelivered elements is determinable, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered element(s) and is recognized as revenue assuming the other revenue recognition criteria are met. In software arrangements in which we do not have VSOE for all undelivered elements, revenue is deferred until fair value is determined or all elements for which we do not have VSOE have been delivered. Alternatively, if sufficient VSOE does not exist and the only undelivered element is services that do not involve significant modification or customization of the software, the entire fee is recognized over the period during which the services are expected to be performed.

Software Licenses

We recognize the revenue allocable to software licenses and specified upgrades upon delivery of the software product or upgrade to the customer, unless the fee is not fixed or determinable or collectability is not probable. If the fee is not fixed or determinable, including new customers whose payment terms are three months or more from shipment, revenue is generally recognized as payments become due from the customer. If collectability is not considered probable, revenue is recognized when the fee is collected. Arrangements that include software services, such as training or installation, are evaluated to determine whether those services are essential to the product's functionality.

A majority of our software arrangements involve "off-the-shelf" software. We consider software to be off-the-shelf software if it can be added to an arrangement with minor changes in the underlying code and it can be used by the customer for the customer's purpose upon installation. For off-the-shelf software arrangements, we recognize the software license fee as revenue after delivery has occurred, customer acceptance is reasonably assured, that portion of the fee represents a non-refundable enforceable claim and is probable of collection, and the remaining services such as training are not considered essential to the product's functionality.

For arrangements that involve significant production, modification or customization of the software, or where software services are otherwise considered essential, we recognize revenue using contract accounting. We generally use the percentage-of-completion method to recognize revenue from these arrangements. We measure progress-to-completion primarily using labor hours incurred, or value added. The percentage-of-completion method generally results in the recognition of reasonably consistent profit margins over the life of a contract because we have the ability to produce reasonably dependable estimates of contract billings and contract costs. We use the level of profit margin that is most likely to occur on a contract. If the most likely profit margin cannot be precisely determined, the lowest probable level of profit in the range of estimates is used until the results can be estimated more precisely. These arrangements are often implemented over an extended time period and occasionally require us to revise total cost estimates. Amounts recognized in revenue are calculated using the progress-to-completion measurement after giving effect to any changes in our cost estimates. Changes to total estimated contract costs, if any, are recorded in the period they are determined. Estimated losses on uncompleted contracts are recorded in the period in which we first determine that a loss is apparent.

For arrangements that include new product releases for which it is difficult to estimate final profitability except to assume that no loss will ultimately be incurred, we recognize revenue under the completed contract method. Under the completed contract method, revenue is recognized only when a contract is completed or substantially complete. Historically these amounts have been immaterial.

Subscription-Based Services

Subscription-based services primarily consist of revenues derived from application service provider ("ASP") arrangements and other hosted service offerings, software subscriptions and disaster recovery services.

We recognize revenue for ASP and other hosting services, software subscriptions, term license arrangements with renewal periods of twelve months or less and disaster recovery ratably over the period of the applicable agreement as services are provided. Disaster recovery agreements and other hosting services are typically renewable annually. ASP and software subscriptions are typically for periods of three to six years and automatically renew unless either party cancels the agreement. The majority of the ASP and other hosting services and software subscriptions also include professional services as well as maintenance and support. In certain ASP arrangements, the customer also acquires a license to the software.

For ASP and other hosting arrangements, we evaluate whether each of the elements in these arrangements represents a separate unit of accounting, as defined by ASC 605-25, Multiple Element Arrangements and ASC 985-605, Software Revenue Recognition, using all applicable facts and circumstances, including whether (i) we sell or could readily sell the element unaccompanied by the other elements, (ii) the element has stand-alone value to the customer, (iii) there is objective reliable evidence of the fair value of the undelivered item, and (iv) there is a general right of return. We consider the applicability of ASC 605-55-121 and 122 with respect to arrangements that include the right to use software stored on another entity's hardware on a contract-by-contract basis. In hosted term-based agreements, where the customer does not have the contractual right to take possession of the software, hosting fees are recognized on a monthly basis over the term of the contract commencing when the customer has access to the software. For professional services associated with hosting arrangements that we determine do not have stand-alone value to the customer, we recognize the services revenue ratably over the remaining contractual period once hosting has gone live and we may begin billing for the hosting services. We record amounts that have been invoiced in accounts receivable and in deferred revenue or revenues, depending on whether the revenue recognition criteria have been met.

If we determine that the customer has the contractual right to take possession of our software at any time during the hosting period without significant penalty, and can feasibly maintain the software on the customer's hardware or enter into another arrangement with a third party to host the software, we recognize the license, professional services and hosting services revenues pursuant to ASC 985-605, Software Revenue Recognition.

Software Services

Some of our software arrangements include services considered essential for the customer to use the software for the customer's purposes. For these software arrangements, both the software license revenue and the services revenue are recognized as the services are performed using the percentage-of-completion contract accounting method. When software services are not considered essential, the fee allocable to the service element is recognized as revenue as we perform the services.

Computer Hardware Equipment

Revenue allocable to computer hardware equipment, which is based on VSOE, is recognized when we deliver the equipment and collection is probable.

Postcontract Customer Support

Our customers generally enter into PCS agreements when they purchase our software licenses. Our PCS agreements are typically renewable annually. Revenue allocated to PCS is recognized on a straight-line basis over the period the PCS is provided. All significant costs and expenses associated with PCS are expensed as incurred. Fair value for the maintenance and support obligations for software licenses is based upon the specific sale renewals to customers.

Allocation of Revenue in Statement of Operations

In our statement of operations, we allocate revenue to software licenses, software services, maintenance and hardware and other based on the VSOE of fair value for elements in each revenue arrangement and the application of the residual method for arrangements in which we have established VSOE of fair value for all undelivered elements. In arrangements where we are not able to establish VSOE of fair value for all undelivered elements, revenue is first allocated to any undelivered elements for which VSOE of fair value has been established. We then allocate revenue to any undelivered elements for which VSOE of fair value has not been established based upon management's best estimate of fair value of those undelivered elements and apply a residual method to determine the license fee. Management's best estimate of fair value of undelivered elements for which VSOE of fair value has not been established is based upon the VSOE of similar offerings and other objective criteria.

Appraisal Services:

For our property appraisal projects, we recognize revenue using the proportionate performance method of revenue recognition since many of these projects are implemented over one to three year periods and consist of various unique activities. Under this method of revenue recognition, we identify each activity for the appraisal project, with a typical project generally calling for bonding, office set up, training, routing of map information, data entry, data collection, data verification, informal hearings, appeals and project management. Each activity or act is specifically identified and assigned an estimated cost. Costs which are considered to be associated with indirect activities, such as bonding costs and office set up, are expensed as incurred. These costs are typically billed as incurred and are recognized as revenue equal to cost. Direct contract fulfillment activities and related supervisory costs such as data collection, data entry and verification are expensed as incurred. The direct costs for these activities are determined and the total contract value is then allocated to each activity based on a consistent profit margin. Each activity is assigned a consistent unit of measure to determine progress towards completion and revenue is recognized for each activity based upon the percentage complete as applied to the estimated revenue for that activity. Progress for the fulfillment activities is typically based on labor hours or an output measure such as the number of parcel counts completed for that activity. Estimated losses on uncompleted contracts are recorded in the period in which we first determine that a loss is apparent.

Other:

The majority of deferred revenue consists of unearned support and maintenance revenue that has been billed based on contractual terms in the underlying arrangement with the remaining balance consisting of payments received in advance of revenue being earned under software licensing, subscription-based services, software and appraisal services and hardware installation. Unbilled revenue is not billable at the balance sheet date but is recoverable over the remaining life of the contract through billings made in accordance with contractual agreements. The termination clauses in most of our contracts provide for the payment for the fair value of products delivered and services performed in the event of an early termination.

Prepaid expenses and other current assets include direct and incremental costs, consisting primarily of commissions associated with arrangements for which revenue recognition has been deferred and third party subcontractor payments. Such costs are expensed at the time the related revenue is recognized.

USE OF ESTIMATES

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. Significant items subject to such estimates and assumptions include the application of the percentage-of-completion and proportionate performance methods of revenue recognition, the carrying amount and estimated useful lives of intangible assets, determination of share-based compensation expense and valuation allowance for receivables. Actual results could differ from estimates.

PROPERTY AND EQUIPMENT, NET

Property, equipment and purchased software are recorded at original cost and increased by the cost of any significant improvements after purchase. We expense maintenance and repairs when incurred. Depreciation and amortization is calculated using the straight-line method over the shorter of the asset's estimated useful life or the term of the lease in the case of leasehold improvements. For income tax purposes, we use accelerated depreciation methods as allowed by tax laws.

RESEARCH AND DEVELOPMENT COSTS

We expensed research and development costs of $11.2 million during 2009, $7.3 million during 2008 and $4.4 million during 2007. We reduced our research and development expense by approximately $3.5 million in 2009, $1.8 million in 2008 and $1.6 million in 2007, which was the amount earned under the terms of our strategic alliance with a development partner.

INCOME TAXES

Income taxes are accounted for under the asset and liability method. Deferred taxes arise because of different treatment between financial statement accounting and tax accounting, known as "temporary differences." We record the tax effect of these temporary differences as "deferred tax assets" (generally items that can be used as a tax deduction or credit in the future periods) and "deferred tax liabilities" (generally items that we received a tax deduction for, which have not yet been recorded in the income statement). The deferred tax assets and liabilities are measured using enacted tax rules and laws that are expected to be in effect when the temporary differences are expected to be recovered or settled. A valuation allowance would be established to reduce deferred tax assets if it is likely that a deferred tax asset will not be realized.

SHARE-BASED COMPENSATION

We have a stock option plan that provides for the grant of stock options to key employees, directors and non-employee consultants. Stock options vest after three to five years of continuous service from the date of grant and have a contractual term of ten years. We account for share-based compensation utilizing the fair value recognition pursuant to ASC 718, Stock Compensation. See Note 10 – "Share-Based Compensation" for further information.

GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill

We have used the purchase method of accounting for all of our business combinations. Our business acquisitions result in the allocation of the purchase price to goodwill and other intangible assets. We first allocate the cost of acquired companies to identifiable assets based on estimated fair values. The excess of the purchase price over the fair value of identifiable assets acquired, net of liabilities assumed, is recorded as goodwill.

We review goodwill impairment annually as of April or more frequently whenever events or changes in circumstances indicate its carrying value may not be recoverable. We have identified two reporting units for impairment testing. Our reporting units are the same as our reportable segments and consistent with the reporting units tested for impairment in prior years. Assets, liabilities and goodwill have been assigned to reporting units based on assets acquired and liabilities assumed as of the date of acquisition.

The provisions of ASC 350, Intangibles — Goodwill and Other, require that we perform a two-step impairment test on goodwill. In the first step, we compare the fair value of each reporting unit to its carrying value. If the fair value of the reporting unit exceeds the carrying value of the net assets assigned to that unit, goodwill is not considered impaired and we are not required to perform further testing. If the carrying value of the net assets assigned to the reporting unit exceeds the fair value of the reporting unit, then we must perform the second step of the impairment test in order to determine the implied fair value of the reporting unit's goodwill. If the carrying value of a reporting unit's goodwill exceeds the asset's implied fair value, then we would record an impairment loss equal to the difference. The fair values calculated in our impairment tests are determined using discounted cash flow models involving several assumptions. These assumptions include, but are not limited to, anticipated operating income growth rates, our long-term anticipated operating income growth rate and the discount rate. Our cash flow forecasts are based on

assumptions that are consistent with the plans and estimates we are using to manage the underlying businesses. The assumptions that are used are based upon what we believe a hypothetical marketplace participant would use in estimating fair value. We evaluate the reasonableness of the fair value calculations of our reporting units by comparing the total of the fair value of all of our reporting units to our total market capitalization. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain. A significant amount of judgment is involved in determining if an indicator of impairment has occurred between testing dates. Such indicators may include, among others: a significant decline in expected future cash flows; a sustained, significant decline in stock price and market capitalization; a significant adverse change in legal factors or in the business climate; unanticipated competition; and reductions in growth rates. In addition, products, capabilities, or technologies developed by others may render our software products obsolete or non-competitive. Any adverse change in these factors could have a significant impact on the recoverability of goodwill. Our annual goodwill impairment analysis, which we performed during the second quarter of 2009, did not result in an impairment charge.

Other Intangible Assets

We make judgments about the recoverability of purchased intangible assets other than goodwill whenever events or changes in circumstances indicate that an impairment may exist. Customer base constitutes approximately 80% of our purchased intangible assets other than goodwill. We review our customer turnover each year for indications of impairment. Our customer turnover has historically been very low (approximately 2%). If indications of impairment are determined to exist, we measure the recoverability of assets by a comparison of the carrying amount of the asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of the assets exceeds their estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the assets exceeds the fair value of the assets. There have been no significant impairments of intangible assets in any of the periods presented.

IMPAIRMENT OF LONG-LIVED ASSETS

We periodically evaluate whether current facts or circumstances indicate that the carrying value of our property and equipment or other long-lived assets to be held and used may not be recoverable. If such circumstances are determined to exist, we measure the recoverability of assets to be held and used by a comparison of the carrying amount of the asset or appropriate grouping of assets and the estimated undiscounted future cash flows expected to be generated by the assets. If the carrying amount of the assets exceeds their estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet. There have been no significant impairments of long-lived assets in any of the periods presented.

COSTS OF COMPUTER SOFTWARE

We capitalize software development costs upon the establishment of technological feasibility and prior to the availability f the product for general release to customers. We did not capitalize any software development costs in 2009 or 2008. We capitalized software development costs of approximately $167,000 during 2007. Software development costs primarily consist of personnel costs and rent for related office space. We begin to amortize capitalized costs when a product is available for general release to customers. Amortization expense is determined on a product-by-product basis at a rate not less than straight-line basis over the product's remaining estimated economic life, but not to exceed five years. Amortization of software development costs was approximately $743,000 in 2009, $4.7 million in 2008, and $4.6 million in 2007, and is included in cost of software license revenue in the accompanying statements of operations.

FAIR VALUE OF FINANCIAL INSTRUMENTS

Cash and cash equivalents, accounts receivables, accounts payables, short-term obligations, deferred revenues and certain other assets at cost approximate fair value because of the short maturity of these instruments. Our investments available-for-sale are recorded at fair value as of December 31, 2009 based upon the level of judgment associated with the inputs used to measure their fair value. See Note 3 – "Fair Value of Financial Instruments" for further information.

CONCENTRATIONS OF CREDIT RISK AND UNBILLED RECEIVABLES

Financial instruments that potentially subject us to significant concentrations of credit risk consist principally of cash and cash equivalents, investments in auction rate securities and accounts receivable from trade customers. Our cash and cash equivalents primarily consists of money market fund investments which are maintained at one major financial institution and the balances often exceed insurable amounts. As of December 31, 2009 we had cash and cash equivalents (including restricted cash) of $15.7 million. We perform periodic evaluations of the credit standing of this financial institution.

Concentrations of credit risk with respect to receivables are limited due to the size and geographical diversity of our customer base. Historically, our credit losses have not been significant. As a result, we do not believe we have any significant concentrations of credit risk as of December 31, 2009.

We maintain allowances for doubtful accounts and sales adjustments, which are provided at the time the revenue is recognized. Since most of our customers are domestic governmental entities, we rarely incur a loss resulting from the inability of a customer to make required payments. Events or changes in circumstances that indicate that the carrying amount for the allowances for doubtful accounts and sales adjustments may require revision, include, but are not limited to, deterioration of a customer's financial condition, failure to manage our customer's expectations regarding the scope of the services to be delivered, and defects or errors in new versions or enhancements of our software products. The following table summarizes the changes in the allowances for doubtful accounts and sales adjustments:

Years ended December 31,	2009	2008	2007
Balance at beginning of year	$ 2,115	$ 1,851	$ 2,971
Provisions for losses – accounts receivable	1,538	1,764	753
Collection of accounts previously written off	—	10	—
Deductions for accounts charged off or credits issued	(1,264)	(1,510)	(1,873)
Balance at end of year	$ 2,389	$ 2,115	$ 1,851

The termination clauses in most of our contracts provide for the payment for the fair value of products delivered or services performed in the event of early termination. Our property appraisal outsourcing service contracts can range up to three years and, in a few cases, as long as five years in duration. In connection with these contracts, as well as certain software service contracts, we may perform work prior to when the software and services are billable and/or payable pursuant to the contract. We have historically recorded such unbilled receivables (costs and estimated profit in excess of billings) in connection with (1) property appraisal services contracts accounted for using proportionate performance accounting in which the revenue is earned based upon activities performed in one accounting period but the billing normally occurs shortly thereafter and may span another accounting period; (2) software services contracts accounted for using the percentage-of-completion method of revenue recognition using labor hours as a measure of progress towards completion in which the services are performed in one accounting period but the billing for the software element of the arrangement may be based upon the specific phase of the implementation; (3) software revenue for which we have objective evidence that the customer-specified objective criteria has been met but the billing has not yet been submitted to the customer; (4) some of our contracts provide for an amount to be withheld from a progress billing (generally a 10% retention) until final and satisfactory project completion is achieved; and (5) in a limited number of cases, we may grant extended payment terms generally to existing customers with whom we have a long-term relationship and favorable collection history.

In connection with this activity, we have recorded unbilled receivables of $13.8 million and $11.2 million at December 31, 2009 and 2008, respectively. We also have recorded retention receivable of $4.0 million at both December 31, 2009 and 2008 and these retentions become payable upon the completion of the contract or completion of our field work and formal hearings. Unbilled receivables and retention receivables expected to be collected in excess of one year have been classified as accounts receivable, long-term portion in the accompanying balance sheets.

INDEMNIFICATION

Most of our software license agreements indemnify our customers in the event that the software sold infringes upon the intellectual property rights of a third party. These agreements typically provide that in such event we will either modify or replace

the software so that it becomes non-infringing or procure for the customer the right to use the software. We have recorded no liability associated with these indemnifications, as we are not aware of any pending or threatened infringement actions that are possible losses. We believe the estimated fair value of these intellectual property indemnification clauses is minimal.

We have also agreed to indemnify our officers and board members if they are named or threatened to be named as a party to any proceeding by reason of the fact that they acted in such capacity. A form of the indemnification agreement was filed as Exhibit 10.1 to our Form 10-K for the year ended December 31, 2002. We maintain directors' and officers' insurance coverage to protect against any such losses. We have recorded no liability associated with these indemnifications. Because of our insurance coverage, we believe the estimated fair value of these indemnification agreements is minimal.

NEW ACCOUNTING PRONOUNCEMENTS

In September 2009, the Financial Accounting Standards Board issued ASU 2009-13, Multiple Element Arrangements. ASU 2009-13 addresses the determination of when the individual deliverables included in a multiple arrangement may be treated as separate units of accounting. ASU 2009-13 also modifies the manner in which the transaction consideration is allocated across separately identified deliverables and establishes definitions for determining fair value of elements in an arrangement. This new update is effective for fiscal years beginning on or after June 15, 2010. Early adoption is allowed. The new standard may impact our application service provider arrangements to recognize revenues, such as installation and data conversion, which are generally provided at the beginning of the arrangement as incurred instead of ratably over the life of the initial hosting term. The adoption of this standard is not expected to have a material impact on our financial condition or results of operation.

(2) ACQUISITIONS

On July 16, 2009, we completed the acquisition of certain assets of KPL, Inc. d/b/a Parker-Lowe & Associates ("Parker-Lowe") for $700,000 in cash. Parker-Lowe provides scanning and retrieval software and related services for land record and social services offices in local governments primarily in the North Carolina area. This acquisition was accounted for as a purchase of a business.

On April 3, 2009, we completed the acquisition of all of the capital stock of Assessment Evaluation Services, Inc. ("AES"). AES develops integrated property appraisal solutions and specializes in applications that deal with the unique provisions of the California Revenue and Taxation Code. The purchase price was approximately $1.1 million in cash.

In connection with these transactions we acquired total tangible assets of approximately $480,000 and assumed total liabilities of approximately $835,000, including $450,000 for contingent consideration for which we have paid $38,000 as of December 31, 2009. The remaining contingent consideration is expected to be paid over the next two years. We recorded goodwill of approximately $1.3 million, all of which is expected to be deductible for tax purposes, and other intangible assets of approximately $820,000. The $820,000 of intangible assets is attributable to acquired software and customer relationships that will be amortized over a weighted average period of approximately 9 years. Our balance sheet as of December 31, 2009 reflects the allocation of the purchase price to the assets acquired and liabilities assumed based on their estimated fair values at the dates of acquisition.

The operating results of these acquisitions are included in our results of operations since the date of acquisition. We believe these acquisitions will complement our business by expanding our presence in certain geographic areas and adding to our customer base.

In 2009, we also paid approximately $1.1 million for certain software assets to complement our tax and appraisal solutions and our student information management solutions.

In August 2008, we completed the acquisition of all the capital stock of School Information Systems, Inc., which develops and sells a full suite of student information and financial management systems for K-12 schools. The purchase price, including transaction costs and excluding cash balances acquired, was approximately $9.9 million in cash and approximately 70,000 shares of Tyler common stock valued at $1.2 million.

In the first quarter of 2008, we completed the acquisitions of all of the capital stock of VersaTrans Solutions Inc. ("VersaTrans") and certain assets of Olympia Computing Company, Inc. d/b/a Schoolmaster ("Schoolmaster"). VersaTrans is a provider of student transportation management software solutions for school districts and school transportation providers across North America, including solutions for school bus routing and planning, redistricting, GPS fleet tracking, fleet maintenance and field trip planning. Schoolmaster provides a full suite of student information systems, which manage such functions as grading, attendance, scheduling, guidance, health, admissions and fund raising. The combined purchase price for these transactions excluding cash acquired and including transaction costs was approximately $13.9 million in cash and approximately 126,000 shares of Tyler common stock valued at $1.7 million.

In September 2007, we completed the acquisition of all the capital stock of EDP Enterprises, Inc. ("EDP"), which develops and sells financial and student information and management systems for public school districts in Texas. In February 2007, we completed the acquisition of all of the capital stock of Advanced Data Systems, Inc. ("ADS"), which develops and sells fund accounting solutions, primarily in New England. The combined purchase price, including transaction costs along with an office building used in ADS's business and excluding cash balances acquired, for these acquisitions as well as miscellaneous other software asset purchases was $9.0 million.

(3) FAIR VALUE OF FINANCIAL INSTRUMENTS

Assets recorded at fair value in the balance sheet as of December 31, 2009 are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels, defined by ASC 820, Fair Value Measurements and Disclosures, are directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets, are as follows:

- Level 1 – Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date;
- Level 2 – Inputs other than Level 1 inputs that are either directly or indirectly observable; and
- Level 3 – Unobservable inputs, for which little or no market data exist, therefore requiring an entity to develop its own assumptions.

As of December 31, 2009 we held certain items that are required to be measured at fair value on a recurring basis. The following tables summarize the fair value of these financial assets:

	December 31, 2009			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$15,696	$15,696	$ —	$ —
Short-term investments available-for-sale	50	50	—	—
Non-current investments available-for-sale	1,976	—	—	1,976
	$17,722	$15,746	$ —	$1,976

	December 31, 2008			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 6,844	$ 6,844	$ —	$ —
Short-term investments available-for-sale	775	775	—	—
Non-current investments available-for-sale	3,779	—	—	3,779
	$11,398	$ 7,619	$ —	$3,779

Cash and cash equivalents consist primarily of money market funds with original maturity dates of three months or less, for which we determine fair value through quoted market prices. These money market funds did not experience any declines in fair value in 2009.

Investments available-for-sale consist of two auction rate municipal securities ("ARS") which are collateralized debt obligations supported by municipal and state agencies and do not include mortgage-backed securities. Short-term investments available-for-sale consists of the portion of one of these ARS, which was partially redeemed at par during the period January 1, 2010 through February 22, 2010. These ARS are debt instruments with stated maturities ranging from 22 to 33 years, for which the interest rate is designed to be reset through Dutch auctions approximately every 30 days. However, due to events in the credit markets, auctions for these securities have not occurred since February 2008. Both of our ARS have had very small partial redemptions at par in the period from July 2009 through February 2010. As of December 31, 2009 we have continued to earn and collect interest on both of our ARS.

Because quoted prices in active markets are no longer available we determined the estimated fair values of these securities utilizing a discounted trinomial model. The model considers the probability of three potential occurrences for each auction event through the maturity date of each ARS. The three potential outcomes for each auction are (i) successful auction/early redemption, (ii) failed auction and (iii) issuer default. Inputs in determining the probabilities of the potential outcomes include but are not limited to, the securities' collateral, credit rating, insurance, issuer's financial standing, contractual restrictions on disposition and the liquidity in the market. The fair value of each ARS is determined by summing the present value of the probability-weighted future principal and interest payments determined by the model. Since there can be no assurances that auctions for these securities will be successful in the near future, we have classified our ARS as non-current investments.

The par and carrying values, and related cumulative unrealized loss for our non-current ARS as of December 31, 2009 are as follows:

	Par Value	Temporary Impairment	Carrying Value
Non-current investments available-for-sale	$2,600	$624	$1,976

In association with this estimate of fair value, we have recorded an after-tax temporary unrealized loss on our non-current ARS of $18,000, net of related tax effects of $10,000 in 2009, which is included in accumulated other comprehensive loss on our balance sheet. The unrealized loss includes the impact of adjusting previously recorded unrealized losses of approximately $120,000, net of related tax effects of $65,000 as of December 31, 2008 for several ARS which were subsequently redeemed for $2.5 million at par during 2009.

We consider the impairment in our ARS as temporary because we do not have the intent to sell, nor is it more-likely-than-not that we will be required to sell these securities before recovery of their cost basis. We believe that this temporary decline in fair value is due entirely to liquidity issues, because the underlying assets of these securities are supported by municipal and state agencies and do not include mortgage-backed securities, have redemption features which call for redemption at 100% of par value and have a current credit rating of A or AAA. The ratings on the ARS take into account credit support through insurance policies guaranteeing each of the bonds' payment of principal and accrued interest, if it becomes necessary. In addition, both ARS have had very small partial redemptions at par in the period July 2009 through February 2010. Based on our cash and cash equivalents balance of $15.7 million and expected operating cash flows, we do not believe a lack of liquidity associated with our ARS will adversely affect our ability to conduct business, and believe we have the ability to hold the securities throughout the currently estimated recovery period. We will continue to evaluate any changes in the market value of our ARS and in the future, depending upon existing market conditions, we may be required to record an other-than-temporary decline in market value.

The following table reflects the activity for assets measured at fair value using Level 3 inputs for the years ended December 31:

Balance as of December 31, 2007	$ —
Transfers into level 3	5,150
Transfers out of level 3	(775)
Unrealized losses included in accumulated other comprehensive loss	(596)
Balance as of December 31, 2008	3,779
Transfers into level 3	—
Transfers out of level 3	(75)
Purchases, sales, issuances and settlements	(1,700)
Unrealized losses included in accumulated other comprehensive loss	(28)
Balance as of December 31, 2009	$ 1,976

(4) PROPERTY AND EQUIPMENT, NET

Property and equipment, net consists of the following at December 31:

	Useful Lives (years)	2009	2008
Land	—	$ 3,349	$ 3,349
Computer equipment and purchased software	3–5	21,394	19,553
Furniture and fixtures	5	6,467	5,103
Building and leasehold improvements	5–39	26,208	16,248
Transportation equipment	5	329	266
		57,747	44,519
Accumulated depreciation and amortization		(21,997)	(17,997)
Property and equipment, net		$ 35,750	$ 26,522

Depreciation expense was $4.4 million during 2009, $3.5 million during 2008, and $2.8 million during 2007.

We own an office building in Yarmouth, Maine, which is leased to third-party tenants and a building in Lubbock, Texas, for which a small portion is leased to a third-party tenant. These leases expire between 2011 and 2015 and are expected to provide rental income of approximately $1.5 million during 2010, $1.1 million during 2011, $628,000 during 2012, $391,000 during 2013, $222,000 during 2014 and $74,000 thereafter. The lease agreements in Yarmouth, Maine, expire between 2011 and 2013, at which time we expect to begin occupying the facility. Rental income associated with these leases was $1.3 million and $662,000 in 2009 and 2008, respectively and was included as a reduction of selling, general and administrative expenses.

(5) GOODWILL AND OTHER INTANGIBLE ASSETS

Intangible assets and related accumulated amortization consists of the following at December 31:

	2009	2008
Gross carrying amount of acquisition intangibles:		
Goodwill	$ 90,258	$ 88,791
Customer related intangibles	39,512	38,887
Software acquired	23,403	22,143
Trade name	1,971	1,971
Lease acquired	1,387	1,387
	156,531	153,179
Accumulated amortization	(35,217)	(30,825)
Acquisition intangibles, net	$ 121,314	$122,354
Post acquisition software development costs	$ 36,701	$ 36,701
Accumulated amortization	(35,986)	(35,243)
Post acquisition software costs, net	$ 715	$ 1,458

Total amortization expense, for acquisition related intangibles and post acquisition software development costs, was $5.1 million during 2009, $9.1 million during 2008, and $8.4 million during 2007.

The allocation of acquisition intangible assets is summarized in the following table:

	December 31, 2009			December 31, 2008		
	Gross Carrying Amount	Weighted Average Amortization Period	Accumulated Amortization	Gross Carrying Amount	Weighted Average Amortization Period	Accumulated Amortization
Non-amortizable intangibles:						
Goodwill	$90,258	—	$ —	$88,791	—	$ —
Amortizable intangibles:						
Customer related intangibles	39,512	18 years	14,022	38,887	18 years	11,449
Software acquired	23,403	5 years	19,900	22,143	5 years	18,489
Trade name	1,971	19 years	879	1,971	19 years	749
Lease acquired	1,387	5 years	416	1,387	5 years	138

The changes in the carrying amount of goodwill for the two years ended December 31, 2009 are as follows:

	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Total
Balance as of December 31, 2007	$ 66,966	$4,711	$ 71,677
Goodwill acquired during the year related to the purchase of VersaTrans	9,278	—	9,278
Goodwill acquired during the year related to the purchase of SIS	6,351	—	6,351
Goodwill acquired during the year related to the purchase of Schoolmaster	1,475	—	1,475
Other	10	—	10
Balance as of December 31, 2008	84,080	4,711	88,791
Goodwill acquired during the year related to the purchase of AES	—	879	879
Goodwill acquired during the year related to the purchase of Parker-Lowe	430	—	430
Other	158	—	158
Balance as of December 31, 2009	$ 84,668	$5,590	$ 90,258

Estimated annual amortization expense relating to acquisition intangibles, including acquired software for which the amortization expense is recorded as cost of revenues and acquired leases for which amortization expense is recorded as selling, general and administrative expenses, is as follows:

Years ending December 31,	
2010	$4,387
2011	3,805
2012	3,538
2013	2,973
2014	2,498

(6) ACCRUED LIABILITIES

Accrued liabilities consist of the following at December 31:

	2009	2008
Accrued wages, bonuses and commissions	$15,945	$13,908
Other accrued liabilities	5,378	5,737
Accrued building construction costs	1,816	—
Accrued health claims	1,551	1,921
Accrued third party contract costs	1,420	1,347
	$26,110	$22,913

(7) SHORT-TERM REVOLVING LINE OF CREDIT

In October 2008, we entered into a revolving bank credit agreement (the "Credit Facility") and a related pledge and security agreement which originally matured October 19, 2009. We amended and extended the related pledge and security agreement in October 2009. The Credit Facility matures October 18, 2010 and provides for total borrowings of up to $25.0 million and a $10.0 million Letter of Credit facility which can either be cash collateralized or issued using availability under the Credit Facility. Borrowings under the Credit Facility bear interest at a rate of either the Wall Street Journal prime rate minus .5% or the 30, 60 or 90-day LIBOR rate plus 2%; however, a minimum interest rate of 3.25% will apply. As of December 31, 2009, our effective interest rate was 3.25% under the Credit Facility. The effective average interest rate for borrowings during the twelve months ended December 31, 2009 was 1.8%. The Credit Facility is secured by substantially all of our assets. The Credit Facility requires us to maintain certain financial ratios and other financial conditions and prohibits us from making certain investments, advances, cash dividends or loans, restricts the amount of our common stock we may purchase and limits incurrence of additional indebtedness and liens. As of December 31, 2009, we were in compliance with those covenants. As of December 31, 2009, we had no outstanding borrowings and unused available borrowing capacity of $23.7 million under the Credit Facility. In addition, as of December 31, 2009, our bank had issued outstanding letters of credit totaling $7.3 million to secure surety bonds required by some of our customer contracts. These letters of credit have been collateralized by restricted cash balances of $6.0 million and $1.3 million of our available borrowing capacity and expire through mid-2010. The carrying amount of the Credit Facility approximates fair value due to the short-term nature of the instrument.

We paid interest of $174,000 in 2009.

(8) INCOME TAX

The income tax provision (benefit) on income from operations consists of the following:

Years ended December 31,	2009	2008	2007
Current:			
Federal	$16,822	$14,320	$10,593
State	2,536	2,245	2,084
	19,358	16,565	12,677
Deferred	(1,730)	(2,151)	(1,598)
	$17,628	$14,414	$11,079

Reconciliation of the U.S. statutory income tax rate to our effective income tax expense rate for operations follows:

Years ended December 31,	2009	2008	2007
Income tax expense at statutory rate	$15,623	$10,247	$10,003
State income tax, net of federal income tax benefit	1,634	1,089	1,321
Non-deductible business expenses	965	3,988	608
Qualified manufacturing activities	(586)	(700)	(490)
Other, net	(8)	(210)	(363)
	$17,628	$14,414	$11,079

In 2008, non-deductible business expenses included the impact of a non-cash legal settlement related to warrants charge of $9.0 million, which was not tax deductible. See Note 14 – "Commitments and Contingencies" for more information.

Approximately 40% of our unvested stock option awards qualify as incentive stock options ("ISOs") for income tax purposes. As such, a tax benefit is not recorded at the time the compensation cost related to the options is recorded for book purposes due to the fact that an ISO does not ordinarily result in a tax benefit unless there is a disqualifying disposition. Stock option grants of non-qualified options result in the creation of a deferred tax asset, which is a temporary difference, until the time that the option is exercised. Due to the treatment of ISOs for tax purposes, our effective tax rate from year to year is subject to variability.

The tax effects of the major items recorded as deferred tax assets and liabilities as of December 31 are:

	2009	2008
Deferred income tax assets:		
Operating expenses not currently deductible	$ 2,068	$ 1,466
Employee benefit plans	3,628	2,528
Capital loss carryforward	230	221
Property and equipment	230	203
Total deferred income tax assets	6,156	4,418
Deferred income tax liabilities:		
Intangible assets	(9,720)	(9,697)
Other	(157)	(181)
Total deferred income tax liabilities	(9,877)	(9,878)
Net deferred income tax liabilities	$(3,721)	$(5,460)

Although realization is not assured, we believe it is more likely than not that all the deferred tax assets at December 31, 2009 and 2008 will be realized. Accordingly, we believe no valuation allowance is required for the deferred tax assets. However, the amount of the deferred tax asset considered realizable could be adjusted in the future if estimates of reversing taxable temporary differences are revised.

No reserves for uncertain income tax positions have been recorded pursuant to ASC 740-10, Income Taxes.

We are subject to U.S. federal tax as well as income tax of multiple state and local jurisdictions. We are no longer subject to United States federal income tax examinations for years before 2006. We are no longer subject to state and local income tax examinations by tax authorities for the years before 2004.

We paid income taxes, net of refunds received, of $18.1 million in 2009, $15.7 million in 2008, and $8.7 million in 2007.

(9) SHAREHOLDERS' EQUITY

The following table details activity in our common stock:

	Years ended December 31,					
	2009		2008		2007	
	Shares	Amount	Shares	Amount	Shares	Amount
Purchases of common stock	(1,235)	$(17,000)	(4,283)	$(58,984)	(1,250)	$(16,163)
Stock option exercises	425	2,295	379	1,815	878	3,589
Employee stock plan purchases	115	1,428	101	1,190	100	1,117
Shares issued for acquisitions	—	—	196	2,863	—	—
Shares issued in connection with legal settlement	—	—	802	11,050	—	—

Subsequent to December 31, 2009 and through February 22, 2010, we repurchased 59,000 shares for an aggregate purchase price of $1.1 million. As of February 22, 2010 we had authorization from our board of directors to repurchase up to 2.2 million additional shares of our common stock.

In 2008, we settled outstanding litigation related to two Stock Purchase Warrants owned by Bank of America, N. A. ("BANA"). In July 2008, as a result of this settlement, BANA paid us $2.0 million and we issued to BANA 801,883 restricted shares of Tyler common stock. See Note 14 – "Commitments and Contingencies" for further information.

(10) SHARE-BASED COMPENSATION

Share-Based Compensation Plan

We have a stock option plan that provides for the grant of stock options to key employees, directors and non-employee consultants. Stock options vest after three to five years of continuous service from the date of grant and have a contractual

term of ten years. Once options become exercisable, the employee can purchase shares of our common stock at the market price on the date we granted the option. We account for share-based compensation utilizing the fair value recognition pursuant to ASC 718, Stock Compensation.

As of December 31, 2009, there were 176,000 shares available for future grants under the plan from the 11.0 million shares previously approved by the stockholders.

Determining Fair Value of Stock Compensation

Valuation and Amortization Method. We estimate the fair value of share-based awards granted using the Black-Scholes option valuation model. We amortize the fair value of all awards on a straight-line basis over the requisite service periods, which are generally the vesting periods.

Expected Life. The expected life of awards granted represents the period of time that they are expected to be outstanding. As provided by ASC 718-10, Stock Compensation, we use the "simplified" method which is allowed for those companies that cannot reasonably estimate expected life of options based on its historical share option exercise experience. We use the "simplified" method to estimate expected life due to insufficient historical exercise data for the current optionee group. In 2005 we established a practice of granting options to a consistent optionee group. This optionee group has not been in place long enough to generate sufficient historical data to estimate the expected period of time an option award would be expected to be outstanding.

Expected Volatility. Using the Black-Scholes option valuation model, we estimate the volatility of our common stock at the date of grant based on the historical volatility of our common stock.

Risk-Free Interest Rate. We base the risk-free interest rate used in the Black-Scholes option valuation model on the implied yield currently available on U.S. Treasury zero-coupon issues with an equivalent remaining term equal to the expected life of the award.

Expected Dividend Yield. We have not paid any cash dividends on our common stock in the last ten years and we do not anticipate paying any cash dividends in the foreseeable future. Consequently, we use an expected dividend yield of zero in the Black-Scholes option valuation model.

Expected Forfeitures. We use historical data to estimate pre-vesting option forfeitures. We record stock-based compensation only for those awards that are expected to vest.

The following weighted average assumptions were used for options granted:

Years ended December 31,	2009	2008	2007
Expected life (in years)	6.5	6.5	6.5
Expected volatility	37.2%	40.9%	42.6%
Risk-free interest rate	3.1%	3.5%	4.5%
Expected forfeiture rate	3%	3%	3%

The following table summarizes share-based compensation expense related to share-based awards which is recorded in the statement of operations:

Years ended December 31,	2009	2008	2007
Cost of software services, maintenance and subscriptions	$ 540	$ 364	$ 227
Selling, general and administrative expense	4,505	3,456	2,138
Total share-based compensation expense	5,045	3,820	2,365
Tax benefit	(1,233)	(846)	(451)
Net decrease in net income	$ 3,812	$2,974	$1,914

Stock Option Activity

Options granted, exercised, forfeited and expired are summarized as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at December 31, 2006	4,087	$ 5.32		
Granted	773	13.42		
Exercised	(878)	4.09		
Forfeited	(10)	8.29		
Outstanding at December 31, 2007	3,972	7.16		
Granted	1,750	14.38		
Exercised	(379)	4.79		
Forfeited	(34)	10.82		
Outstanding at December 31, 2008	5,309	9.69		
Granted	835	17.25		
Exercised	(425)	5.40		
Forfeited	(15)	7.80		
Outstanding at December 31, 2009	5,704	11.12	7	$50,139
Exercisable at December 31, 2009	2,765	$ 7.50	5	$34,314

As of December 31, 2009, we had unvested options to purchase 2.9 million shares with a weighted average grant date fair value of $6.70. As of December 31, 2009, we had $15.8 million of total unrecognized compensation cost related to unvested options, net of expected forfeitures, which is expected to be amortized over a weighted average amortization period of 3.6 years.

Other information pertaining to option activity was as follows during the twelve months ended December 31:

	2009	2008	2007
Weighted average grant-date fair value of stock options granted	$ 7.38	$ 6.73	$ 6.69
Total fair value of stock options vested	4,346	2,600	1,710
Total intrinsic value of stock options exercised	4,656	3,929	8,793

Employee Stock Purchase Plan

Under our Employee Stock Purchase Plan ("ESPP") participants may contribute up to 15% of their annual compensation to purchase common shares of Tyler. The purchase price of the shares is equal to 85% of the closing price of Tyler shares on the last day of each quarterly offering period. As of December 31, 2009, there were 341,000 shares available for future grants under the ESPP from the 1.0 million shares originally reserved for issuance.

(11) EARNINGS PER SHARE

Basic earnings and diluted earnings per share data were computed as follows:

Years Ended December 31,	2009	2008	2007
Numerator for basic and diluted earnings per share			
Net income	$27,010	$14,862	$17,501
Denominator:			
Weighted-average basic common shares outstanding	35,240	37,714	38,735
Assumed conversion of dilutive securities:			
Stock options	1,384	1,470	1,715
Warrants	—	—	902
Potentially dilutive common shares	1,384	1,470	2,617
Denominator for diluted earnings per share – Adjusted weighted-average shares	36,624	39,184	41,352
Earnings per common share:			
Basic	$ 0.77	$ 0.39	$ 0.45
Diluted	$ 0.74	$ 0.38	$ 0.42

Stock options representing the right to purchase common stock of 2.6 million shares in 2009, 1.6 million shares in 2008, and 128,000 shares in 2007 were not included in the computation of diluted earnings per share because their inclusion would have had an anti-dilutive effect.

(12) LEASES

We lease office facilities for use in our operations, as well as transportation, computer and other equipment. We also have an office facility lease agreement with a shareholder. Most of our leases are non-cancelable operating lease agreements and they expire at various dates through 2014. In addition to rent, the leases generally require us to pay taxes, maintenance, insurance and certain other operating expenses.

Rent expense was approximately $6.3 million in 2009, $5.9 million in 2008, and $4.9 million in 2007, which included rent expense associated with related party lease agreements of $2.0 million in 2009 and $1.8 million in both 2008 and 2007.

Future minimum lease payments under all non-cancelable leases at December 31, 2009 are as follows:

Years ending December 31,	
2010	$ 6,033
2011	5,265
2012	3,954
2013	2,365
2014	1,721
Thereafter	—
	$19,338

Included in future minimum lease payments are non-cancelable payments due to related parties of $1.9 million in 2010, $1.8 million in 2011, $1.7 million in 2012, $1.7 million in 2013, $1.7 million in 2014 and none thereafter.

(13) EMPLOYEE BENEFIT PLANS

We provide a defined contribution plan for the majority of our employees meeting minimum service requirements. The employees can contribute up to 30% of their current compensation to the plan subject to certain statutory limitations. We contribute up to a maximum of 3% of an employee's compensation to the plan. We made contributions to the plan and charged operations $2.6 million during 2009, $2.0 million during 2008, and $1.7 million during 2007.

(14) COMMITMENTS AND CONTINGENCIES

On November 3, 2008, a putative collective action complaint was filed against us in the United States District Court for the Eastern District of Texas (the "Court") on behalf of current and former telephone and remote customer support personnel ("Category 1"), computer hardware and software set up and maintenance personnel ("Category 2"), implementation personnel ("Category 3"), sales support personnel ("Category 4"), and quality assurance analysts ("Category 5"). The petition alleges that we misclassified these groups of employees as "exempt" rather than "non-exempt" under the Fair Labor Standards Act and that we therefore failed to properly pay overtime wages. The suit was initiated by six former employees working out of our Longview, Texas, office and seeks to recover damages in the form of lost overtime pay, liquidated damages equal to the amount of lost overtime pay, interest, costs, and attorneys' fees. On June 23, 2009, the Court issued an Order granting Plaintiffs' motion for conditional certification for the purpose of providing notice to potential plaintiffs about the litigation. Accordingly, the plaintiffs sent the court ordered notice to all current and former employees who worked in the foregoing job classifications at any time from June 23, 2006 until June 23, 2009. On October 26, 2009, the "opt in" period for plaintiffs and potential plaintiffs closed. There are a total of 78 plaintiffs in the litigation consisting of the following: 31 in Category 1; 4 in Category 2; 39 in Category 3; 2 in Category 4; and 2 in Category 5. We intend to vigorously defend the action. Given the preliminary nature of the alleged claims and the inherent unpredictability of litigation, we cannot at this time estimate the possible outcome of any such action.

On June 27, 2008, we settled outstanding litigation related to two Stock Purchase Warrants (the "Warrants") owned by Bank of America, N. A. ("BANA"). As disclosed in prior SEC filings, the Warrants entitled BANA to acquire 1.6 million shares of Tyler common stock at an exercise price of $2.50 per share. The Warrants expired on September 10, 2007. Prior to their expiration, BANA attempted to exercise the Warrants; however, the parties disputed whether or not BANA's exercise was effective. We filed suit for declaratory judgment seeking a court's determination on the matter, and BANA asserted numerous counterclaims against us, including breach of contract and misrepresentation. Following court-ordered mediation, in July 2008, BANA paid us $2.0 million and we issued to BANA 801,883 restricted shares of Tyler common stock. Accordingly, as a result of the settlement, we recorded a non-cash legal settlement related to warrants charge of $9.0 million, which was not tax deductible.

Other than ordinary course, routine litigation incidental to our business and except as described in this Annual Report, there are no material legal proceedings pending to which we are party or to which any of our properties are subject.

(15) SUBSEQUENT EVENTS

On January 6, 2010, we acquired all the assets of Wiznet, Inc. ("Wiznet") for a cash purchase price of $9.5 million. Wiznet provides electronic document filing solutions for courts and law offices throughout the United States and is currently integrated with our primary courts and justice applications. We have not finalized the allocation of the purchase price.

We evaluate events and transactions that occur after the balance sheet date as potential subsequent events. We performed this evaluation through February 25, 2010, the date on which we issued our financial statements.

(16) SEGMENT AND RELATED INFORMATION

We are a major provider of integrated information management solutions and services for the public sector, with a focus on local governments. Factors used to identify our reportable operating segments include the financial information regularly utilized for evaluation by our chief operating decision-maker (CODM) in making decisions about how to allocate resources and in assessing our performance. We have determined that our CODM is our Chief Executive Officer.

We provide our software systems and services and appraisal services through four business units:

- financial management and education software solutions;
- financial management and municipal courts and justice software solutions;
- courts and justice software solutions; and
- appraisal and tax software solutions and property appraisal services.

Historically, we have reported one segment. In 2009 we reexamined the economics of our businesses, and found that the financial metrics for our appraisal and tax software solutions and services unit were becoming dissimilar from our enterprise software solutions units. Accordingly, we now report two segments: (1) Enterprise Software Solutions and (2) Appraisal and Tax Software Solutions and Services. In accordance with ASC 280-10, Segment Reporting, the financial management and education software solutions unit, financial management and municipal courts and justice software solutions unit and the courts and justice software solutions unit meet the criteria for aggregation and are presented in one segment, "Enterprise Software Solutions." The Enterprise Software Solutions segment provides municipal and county governments and schools with software systems to meet their information technology and automation needs for mission-critical "back-office" functions such as financial management and courts and justice processes. The Appraisal and Tax Software Solutions and Services segment provides systems and software that automate the appraisal and assessment of real and personal property as well as property appraisal outsourcing services for local governments and taxing authorities. Property appraisal outsourcing services include: the physical inspection of commercial and residential properties; data collection and processing; computer analysis for property valuation; preparation of tax rolls; community education; and arbitration between taxpayers and the assessing jurisdiction.

We evaluate performance based on several factors, of which the primary financial measure is business segment operating income. We define segment operating income as income before noncash amortization of intangible assets associated with their acquisition, share-based compensation expense, interest expense and income taxes. Segment operating income includes

intercompany transactions. The majority of intercompany transactions relate to contracts involving more than one unit and are valued based on the contractual arrangement. Segment operating income for corporate primarily consists of compensation costs for the executive management team and certain accounting and administrative staff and share-based compensation expense for the entire company. The accounting policies of the reportable segments are the same as those described in Note 1, "Summary of Significant Accounting Policies."

Segment assets include net accounts receivable, prepaid expenses and other current assets, net property and equipment and intangibles associated with their acquisition. Corporate assets consist of cash and investments, prepaid insurance, deferred income taxes and net property and equipment mainly related to unallocated information and technology assets.

Enterprise Software Solutions segment capital expenditures in 2009 and 2008 include $11.2 million and $16.0 million, respectively for the purchase of buildings in connection with plans to consolidate workforces and support long-term growth. 2009 capital expenditures include a $1.8 million accrued retainage payment we expect to pay by mid-2010.

In 2009 and 2008 the Appraisal and Tax Software Solutions and Services segment had one appraisal services customer which accounted for 10.4% and 12.6%, respectively, of this segment's total revenues.

As of and year ended December 31, 2009	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Corporate	Totals
Revenues				
Software licenses	$ 39,910	$ 2,221	$ —	$ 42,131
Subscriptions	16,870	311	—	17,181
Software services	71,176	9,229	—	80,405
Maintenance	114,237	10,275	—	124,512
Appraisal services	—	18,740	—	18,740
Hardware and other	6,248	—	1,069	7,317
Intercompany	1,618	—	(1,618)	—
Total revenues	$250,059	$40,776	$ (549)	$290,286
Depreciation and amortization expense	8,031	608	858	9,497
Segment operating income	55,639	6,949	(13,688)	48,900
Capital expenditures	13,361	192	614	14,167
Segment assets	$220,135	$25,597	$ 24,938	$270,670

As of and year ended December 31, 2008	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Corporate	Totals
Revenues				
Software licenses	$ 39,936	$ 1,554	$ —	$ 41,490
Subscriptions	14,352	22	—	14,374
Software services	65,906	9,091	—	74,997
Maintenance	98,383	9,075	—	107,458
Appraisal services	—	19,098	—	19,098
Hardware and other	6,354	26	1,304	7,684
Intercompany	956	2	(958)	—
Total revenues	$225,887	$38,868	$ 346	$265,101
Depreciation and amortization expense	11,596	510	505	12,611
Segment operating income	47,698	5,448	(11,769)	41,377
Capital expenditures	17,563	420	2,160	20,143
Segment assets	$208,868	$24,409	$ 18,484	$251,761

As of and year ended December 31, 2007	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Corporate	Totals
Revenues				
Software licenses	$ 33,789	$ 1,274	$ —	$ 35,063
Subscriptions	10,406	—	—	10,406
Software services	52,784	7,499	—	60,283
Maintenance	77,012	8,399	—	85,411
Appraisal services	—	21,318	—	21,318
Hardware and other	7,294	21	—	7,315
Intercompany	780	138	(918)	—
Total revenues	$182,065	$38,649	$ (918)	$219,796
Depreciation and amortization expense	10,310	542	359	11,211
Segment operating income	34,833	5,040	(9,336)	30,537
Capital expenditures	2,449	412	817	3,678
Segment assets	$157,981	$22,869	$60,658	$241,508

Reconciliation of reportable segment operating income to the Company's consolidated totals:	2009	2008	2007
Total segment operating income	$48,900	$41,377	$30,537
Amortization of acquired software	(1,411)	(1,799)	(2,279)
Amortization of customer and trade name intangibles	(2,705)	(2,438)	(1,478)
Non-cash legal settlement related to warrants	—	(9,045)	—
Other (expense) income	(146)	1,181	1,800
Income before income taxes	$44,638	$29,276	$28,580

(17) QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

The following table contains selected financial information from unaudited statements of operations for each quarter of 2009 and 2008.

	2009				2008			
Quarters Ended	Dec. 31	Sept. 30	June 30	Mar. 31	Dec. 31	Sept. 30	June 30 (A)	Mar. 31
Revenues	$74,217	$74,332	$72,172	$69,565	$69,544	$68,637	$67,569	$59,351
Gross profit	33,239	33,235	31,997	30,292	28,945	29,950	29,089	21,803
Income before income taxes	10,922	12,421	11,334	9,961	9,845	12,335	2,026	5,070
Net income	6,656	7,475	6,873	6,006	5,131	6,359	246	3,126
Earnings per diluted share	0.18	0.20	0.19	0.16	0.14	0.16	0.01	0.08
Shares used in computing diluted earnings per share	36,600	36,487	36,723	36,747	37,604	40,019	39,633	39,527

(A) On June 27, 2008, we settled outstanding litigation related to two Stock Purchase Warrants (the "Warrants") owned by Bank of America, N. A. ("BANA"). The Warrants entitled BANA to acquire 1.6 million shares of Tyler common stock at an exercise price of $2.50 per share. Following court-ordered mediation, in July 2008, BANA paid us $2.0 million and we issued to BANA 801,883 restricted shares of Tyler common stock. Accordingly, we recorded a non-cash legal settlement related to warrants charge of $9.0 million, which was not tax deductible, during the three months ended June 30, 2008.

Performance Graph

The following table compares total Shareholder returns for Tyler over the last five years to the Standard and Poor's 500 Stock Index and the Standard and Poor's 600 Information Technology Index assuming a $100 investment made on December 31, 2004. Each of the three measures of cumulative total return assumes reinvestment of dividends. The stock performance shown on the graph below is not necessarily indicative of future price performance.

COMPARISON OF CUMULATIVE FIVE YEAR TOTAL RETURN

	2004	2005	2006	2007	2008	2009
Tyler Technologies, Inc.	100	105.02	168.18	154.19	143.30	238.16
S&P 500 Index	100	104.91	121.48	128.16	80.74	102.11
S&P 600 Information Technology Index	100	99.76	109.17	119.32	71.15	105.41

Corporate Officers

John M. Yeaman
Chairman of the Board

John S. Marr, Jr.
President and Chief Executive Officer

Dustin R. Womble
Executive Vice President

Brian K. Miller
Executive Vice President
Chief Financial Officer and Treasurer

H. Lynn Moore, Jr.
Executive Vice President
General Counsel and Secretary

Samantha B. Crosby
Vice President
Marketing

Rick L. Hoff
Vice President
Chief Technology Officer

Robert J. Sansone
Vice President
Human Resources

W. Michael Smith
Vice President
Chief Accounting Officer

Terri L. Alford
Controller

Board of Directors

John M. Yeaman[1]
Chairman of the Board
Tyler Technologies, Inc.

John S. Marr, Jr.[1]
President and Chief Executive Officer
Tyler Technologies, Inc.

Donald R. Brattain[2,3]
President
Brattain and Associates, LLC

J. Luther King, Jr.[2,4]
Chief Executive Officer
Luther King Capital Management

G. Stuart Reeves[2,3,4]
Retired Executive Vice President
Electronic Data Systems Corporation

Michael D. Richards[3,4]
Executive Vice President
Republic Title of Texas, Inc.

Dustin R. Womble[1]
Executive Vice President
Tyler Technologies, Inc.

[1] *Executive Committee*
[2] *Audit Committee*
[3] *Nominating and Governance Committee*
[4] *Compensation Committee*

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Independent Registered Public Accounting Firm

Ernst & Young LLP
Dallas, Texas

Annual Meeting of Stockholders

Our Annual Meeting will be held on Thursday, May 13, 2010, at 9:30 a.m. Central time at The Park City Club, 5956 Sherry Lane, Suite 1700, Dallas, Texas 75225.

Certifications

We submitted an unqualified Annual CEO Certification to the New York Stock Exchange (NYSE) as required by the NYSE Listed Company rules. We also filed with the Securities and Exchange Commission the Chief Executive Officer and Chief Financial Officer certifications required under Section 302 of the Sarbanes-Oxley Act as exhibits to our Annual Report on Form 10-K.

Investor Information

Our Annual Report on Form 10-K is available on the Company's website at www.tylertech.com. A copy of the Form 10-K or other information may also be obtained by contacting the Investor Relations Department at corporate headquarters.

Investor Relations

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Common Stock

Listed on the New York Stock Exchange under the symbol "TYL"

Empowering people who serve the public™

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