



the journey
continues

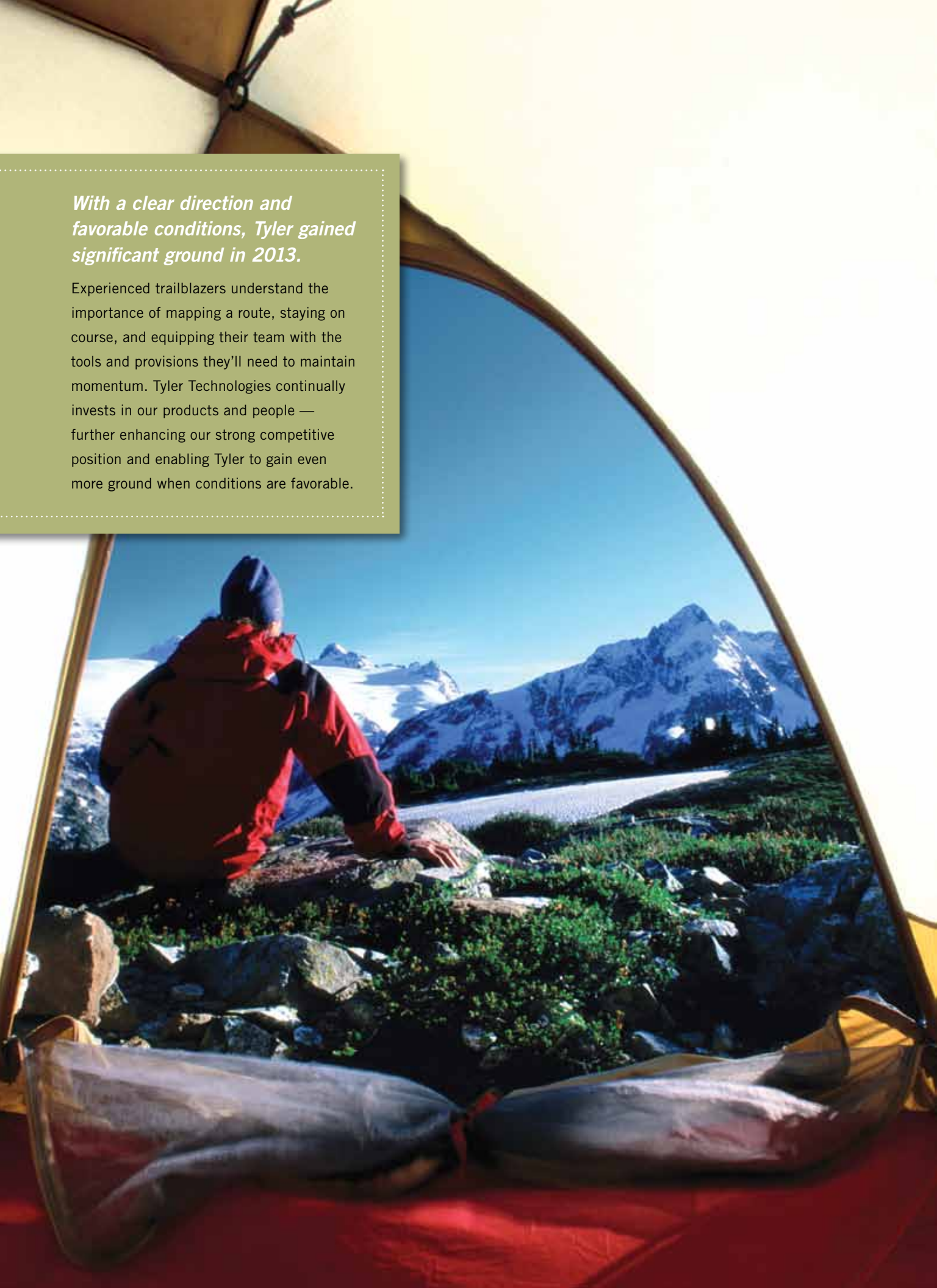


Empowering people who serve the public®

2013 Annual Report

With a clear direction and favorable conditions, Tyler gained significant ground in 2013.

Experienced trailblazers understand the importance of mapping a route, staying on course, and equipping their team with the tools and provisions they'll need to maintain momentum. Tyler Technologies continually invests in our products and people — further enhancing our strong competitive position and enabling Tyler to gain even more ground when conditions are favorable.



to our shareholders

Tyler Technologies takes a steady, long-term approach to our business — building on successes and consistently investing in growth opportunities. In 2013, our commitment to that strategy continued to strengthen our position by magnifying the benefits of an improving market.

Not only did Tyler achieve our best year ever by virtually every financial measure, reaching new highs in revenues, earnings, bookings and backlog, but we did so while investing in emerging opportunities and continuing to improve our competitive position across our product groups. These results reflect our unwavering focus on the core strategy that has served our stakeholders so well over the years.

Financial Highlights

For the second consecutive year, Tyler achieved double-digit growth in revenue — bringing our 2013 total to \$416.6 million, up 14.7 percent over 2012. Recurring revenue from maintenance and subscriptions accounted for 61 percent of total revenue, driven in part by growing client demand for cloud-based software as a service (SaaS) solutions. Subscription revenues rose 39 percent from 2012 as more new and existing clients opted for SaaS delivery, coupled with strong growth in revenue streams such as e-filing for courts.

Bookings grew even faster than revenues, with a 45 percent increase over 2012, pushing year-end backlog up 45 percent to \$551.7 million and enhancing visibility into 2014 and beyond. A great deal of the momentum in bookings and awards in 2013 can be attributed to a growing number of multiyear SaaS agreements, along with a restructured e-filing contract with the state of Texas that replaces transaction-based fees with fixed revenues now included in backlog.

Net income was \$39.1 million, or \$1.13 per diluted share, an increase of 18.5 percent compared to \$33 million, or \$1.00 per diluted share, in 2012. Non-GAAP net income for the year was \$52.3 million, or \$1.51 per diluted share, up 22.9 percent from 2012. We achieved these solid results even as we expensed significant investments in long-term opportunities, including approximately \$3.3 million in startup costs related to our statewide e-filing contract for Texas courts, as well as costs associated with onboarding staff to increase our capacity to deliver current and projected backlog.

Investing for Strength

From an economic perspective, the public sector experienced considerable challenges in recent years that lengthened sales cycles and caused many local governments and schools to delay software purchases in 2010 and 2011. While many of our competitors reacted to the slowdown by cutting back on research and development, Tyler chose to increase our investments in product development to further advance our already strong competitive position.

With many local governments seeing an improved economic environment over the last several quarters, activity in our market has gradually returned to normal levels, and Tyler has emerged from the recession stronger than ever. Win

Tyler's resolute business strategy, combined with a resurgence of public sector activity amid a strengthening economy, generated double-digit revenue growth for the second consecutive year.

rates are up and we are clearly gaining market share. We spent a record \$23.3 million on research and development in 2013 to keep the momentum going. And our client retention rate of approximately 98 percent serves as a powerful testament to our ability to deliver lasting value to the public sector clients we serve.

An Employer of Choice

Tyler's current workforce already reflects an unrivaled level of experience supporting the public sector. In fact, more than 60 percent of employees who were with the company a decade ago are still with Tyler today. As Tyler continues to grow, attracting and retaining talented employees remains a top priority. That's why we offer competitive compensation and benefits, career development opportunities, and a work environment that fosters employee pride. In August 2013, we moved into our new company-owned corporate headquarters in Plano, Texas, which allowed us to

consolidate our Courts & Justice Division and corporate staff from two separate leased spaces in the greater Dallas area. More than 400 employees office here, and the 26-acre campus offers considerable room for future expansion.

We were recognized for the sixth time as one of the Best Places to Work in Maine, where more than 500 Tyler employees are based, and we were ranked among North Texas' Top 100 Places to Work by the *Dallas Morning News*. We were also recognized by the *Dayton Daily News* as one of the Top Workplaces in the Dayton metro area, where our Appraisal & Tax Division is headquartered. These accolades are important to us, in that they reflect our commitment to supporting the professional success and personal well-being of our employees. By strengthening our position as an employer of choice, Tyler continues to lead the industry with innovative, reliable solutions that are helping the public sector do more with less.



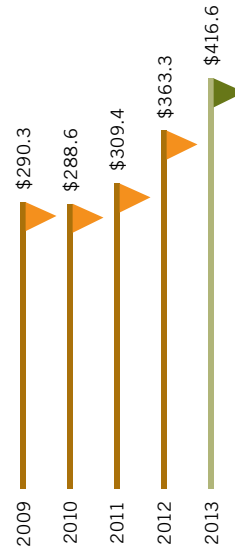
Executing Our Strategies

Through all economic climates, Tyler's core growth strategies endure — expanding our geographic reach, broadening our product and service offerings, winning large-scale contracts, and extending our relationships with existing clients. As we review our 2013 performance and set our sights on the journey ahead, we extend our thanks to the valued shareholders, employees and clients who share our success as the journey continues.

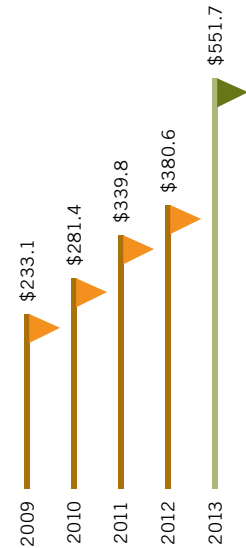
John S. Marr Jr.

President and Chief Executive Officer
March 21, 2014

Total Revenues
in millions



Backlog
in millions



(from left to right)

Brett Cate
Christopher P. Hepburn
Matthew B. Bieri
Terri L. Alford
W. Michael Smith
Brian K. Miller
John M. Yeaman
John S. Marr Jr.
Dustin R. Womble
H. Lynn Moore Jr.
Samantha B. Crosby
Robert J. Sansone
Bruce Graham
Richard E. Peterson Jr.
Andrew D. Teed

For more information about our management team, please refer to the inside back cover.

tyler overview

With more than 2,600 employees and 11,000 government and school clients in all 50 states, Canada, the Caribbean, the United Kingdom, and other international jurisdictions, Tyler Technologies is the largest software company in the nation with an exclusive focus on the public sector. We're more than software developers — we're implementation and support partners whose client relationships span decades. From student transportation management solutions in South Texas to an \$18 million property tax solution for New York City, Tyler's perpetual upgrades and comprehensive services empower our clients to serve the public with efficiency, accessibility and fiscal responsibility.

SCHOOL SOLUTIONS



STUDENT MANAGEMENT

Tyler offers a full suite of student management solutions to help educators and administrators put students first, including student information (grades, attendance and scheduling), data analytics, special education and student transportation. In fact, Tyler's Versatrans® solutions manage transportation for 1 out of every 10 U.S. school districts.



FINANCIAL

Tyler delivers integrated financial solutions that address the unique budgeting and procurement needs of educational clients. By enhancing our clients' most essential business functions, Tyler helps schools maximize their resources in the more than 1,350 school districts we serve.

STATE & LOCAL GOVERNMENT SOLUTIONS



ERP / FINANCIAL

More than 4,000 government entities rely on Tyler's financial solutions for efficient management of their accounting, payroll and human resources functions as they manage \$116 billion in public sector funds annually. Our human capital management solutions process paychecks for more than 1 million public sector employees.



COURTS & JUSTICE

From paperless court case management to e-filing solutions, Tyler's courts and justice products offer a broad range of functionality for courts, prosecutors, law enforcement, corrections and supervision staff. More than 25 percent of the U.S. population lives in jurisdictions that have licensed Tyler's Odyssey® case management or e-filing solutions.



APPRAISAL & TAX

Tyler serves 1,300 taxing authorities throughout the United States and Canada with computer-assisted mass appraisal (CAMA) solutions, tax billing and collections software, and turnkey reassessment and revaluation services. Tyler's appraisal and tax solutions facilitate the efficient management of more than 60 million parcels of property.



PUBLIC SAFETY

When it comes to public safety, timeliness and accuracy are paramount. Tyler's public safety solutions facilitate the sharing of mission-critical information and streamline records management for first responders, dispatchers, jails and others. Protecting more than 2 million citizens every day, Tyler solutions equip jurisdictions to take 1.6 million 911/dispatch calls annually.



PLANNING, PERMITTING & LICENSING

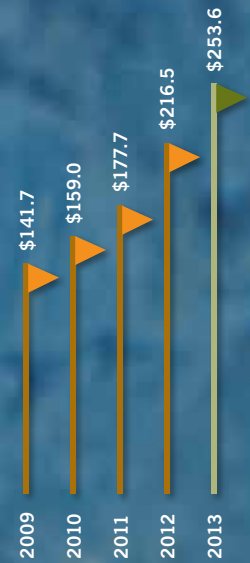
Tyler's planning, permitting and licensing products centralize and connect processes across building departments, code enforcement, public works and other agencies, with 24-hour citizen access and mobile solutions that extend functionality into the field. These solutions serve approximately 23 million citizens in the United States and Canada.



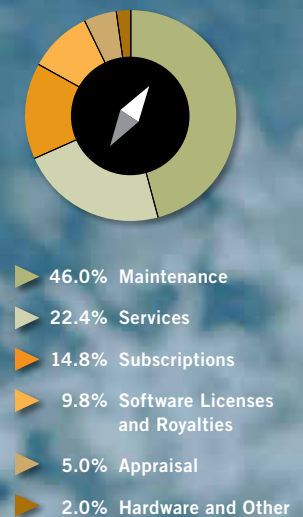
RECORDS & DOCUMENTS

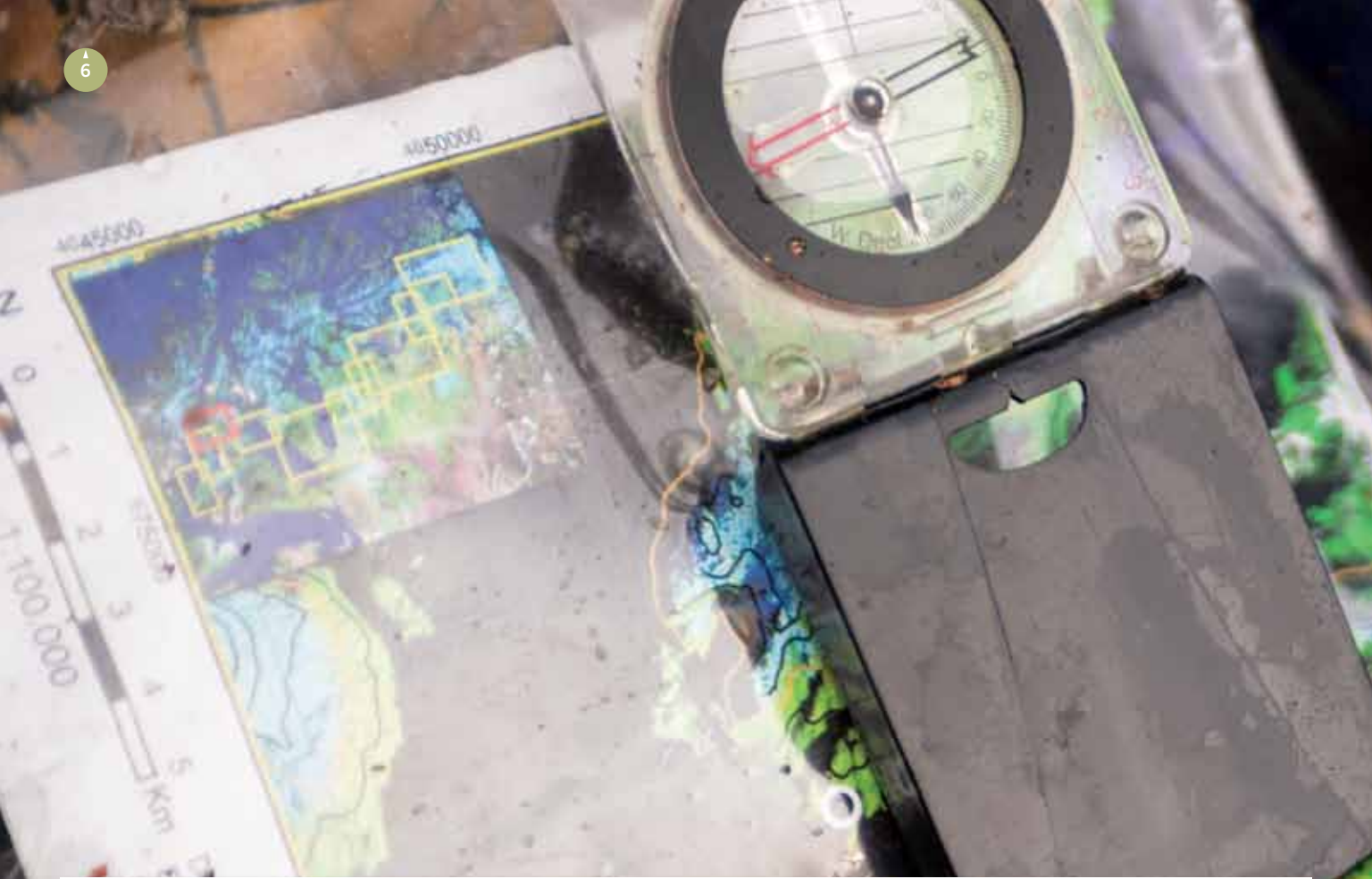
Our records and documents solutions are instrumental in the management of land and vital records for 24 million citizens across the United States. Using Tyler solutions, our clients currently store and access more than 380 million land and vital records.

Recurring Revenues
in millions



Revenue Mix





Q&A:

Tyler's strong competitive position contributed to accelerating growth and profitability in 2013 as the broader public sector market continued to improve. In this question and answer format, we address many of the issues and events that shaped our performance during the year and will continue to influence the future.

How would you characterize the public sector market in 2013?

In our 2012 annual report, we noted that the markets we serve were gradually improving following a challenging new-business environment in 2010 and 2011, as many local governments and schools experienced budget pressures in a weak economy. That improvement continued into 2013, and by year-end market activity had returned to pre-recession levels not seen since 2009. As we enter 2014, our pipeline of new business opportunities is at a historically high level.

How did Tyler benefit from the improved economic environment, and what other factors contributed to Tyler's record results in 2013?

While the improved economic environment certainly contributed to Tyler's revenue and earnings increases in 2013, our growth was clearly above the market growth rate, as bookings and year-end backlog each rose by 45 percent over 2012. We attribute that market share gain to our strong competitive position, which reflects increased investments in product development over the past several years as well as an unmatched record of successfully executing projects on time and on budget.

mapping the route

Tyler's core strategies serve as a compass for the decisions we make. By expanding our geographic reach, broadening our product offerings, winning large-scale contracts, and extending our relationships with existing clients, we continue to move forward with confidence.

In previous reports, you've discussed a trend toward software as a service (SaaS) solutions. Did this hold true for 2013 as well?

The number of clients choosing Tyler's SaaS solutions continued to rise in 2013. In fact, subscriptions — including SaaS and e-filing for courts as well as other transaction-based offerings — were the fastest-growing part of our business in 2013. Subscriptions were up 39 percent as 100 new clients signed SaaS contracts and 63 existing Tyler clients converted from on-premises solutions. Thirty-two percent of our new-name clients chose SaaS solutions in 2013, compared to 30 percent of new clients in 2012.

There are a number of reasons why Tyler's cloud offerings have increasing appeal. All of our major products are available as robust SaaS solutions that offer the same features, functionality and evergreen upgrades as our on-premises solutions. This gives clients the option to easily convert from one model to the other without disruption. Additionally, SaaS solutions enable clients to spread out their investments over a longer period of time — which can be an attractive option for clients who need to replace mission-critical functions, but are challenged with funding



ERP | FINANCIAL

We continued to expand our leadership position in local government financial systems with both the Incode® and Munis® suites of products, along with Microsoft Dynamics® AX. We offered our first Windows 8 apps on the Microsoft store — Munis Field Inspector, Munis My Work and Munis Work Orders. We also launched the general release of CAFR Statement Builder and Tyler eTimekeeper.

Contract highlights for on-premises license implementations included a \$4.4 million Munis and EnerGov® deal with the city of Columbia, Missouri; a \$4.3 million contract with Pasco County, Florida; and significant contracts with El Paso County, Texas, and Pasadena, California. Major new SaaS clients included a \$4.1 million Munis contract with Baltimore County, Maryland; and a new arrangement with Hallandale Beach, Florida.

We also signed five new clients for Microsoft Dynamics AX, led by a \$5 million contract with the city of Columbus, Ohio, the nation's 15th-largest city.

major capital investments. Our SaaS solutions also enable local governments to deal effectively with the “brain-drain” that many of them face as longtime employees retire and it becomes more difficult to manage their increasingly complex IT infrastructures.

How does the growing popularity of the cloud affect Tyler’s financial model?

Although the percentage of new clients choosing our SaaS model continues to increase, it has done so gradually over the past decade and we expect that to continue in the near future. Because the shift is gradual, the effect of the ongoing transition of our model is not disruptive. We have still been able to achieve margin improvements while growing recurring revenue streams, as the lower first-year

margins on new SaaS clients are offset by higher margins from SaaS clients added in prior years. We believe the fact that we offer our solutions in both traditional on-premises and hosted cloud solution models differentiates Tyler from most of our competitors. Simply put, we want to win new clients and serve their needs, regardless of their preference for how they acquire and access our software.

With the increasing adoption of SaaS solutions, how are traditional software licenses performing?

As noted above, the transition to SaaS in our market is slower than in the private sector, and more than two-thirds of our new clients in 2013 chose a traditional license-based, on-premises solution. In fact, software license and royalties revenues increased more than 20 percent in 2013 to reach the highest level in four years, even as subscription



With eFileTexas.gov, Texas courts were well prepared for mandatory e-filing

On January 1, 2014, the state of Texas initiated a rolling schedule that will make electronic filing mandatory for all civil court cases in Texas by 2016. Tyler expects to eventually serve 90,000 attorneys and all 254 counties in Texas through the eFileTexas.gov site, which was successfully launched in 2013. The system shortens lines at clerk counters, enhances tracking and reporting, and saves taxpayer dollars through increased efficiencies associated with the elimination of paper documents.



COURTS & JUSTICE

Our Courts & Justice Division went live with two major Odyssey jail software implementations in 2013 — Fulton County (Atlanta), Georgia; and El Paso County, Texas.

Three new statewide Odyssey deals led our Courts & Justice Division signings in 2013, including a \$19.2 million contract with the state of Washington; a \$6.2 million deal with Idaho; and a \$5.9 million contract with Rhode Island. Tyler also continued to gain ground in the California courts market, winning 12 of the 14 contracts awarded in the state as of this writing.

Significant new clients for our Incode municipal court solution included the cities of Corpus Christi, Texas; and Pueblo, Colorado.

revenues grew 39 percent. In a sense, Tyler is a hybrid company committed to both SaaS and traditional software license offerings — providing our shareholders with a fast-growing SaaS business built on top of a mature, highly profitable license-based software business with more than 11,000 installations and a maintenance base that should surpass \$200 million in revenues in 2014. No matter which delivery method a client may choose, these long-term client relationships hold tremendous value as we generate recurring revenues and cultivate client loyalty with a high level of client support and perpetual upgrades.

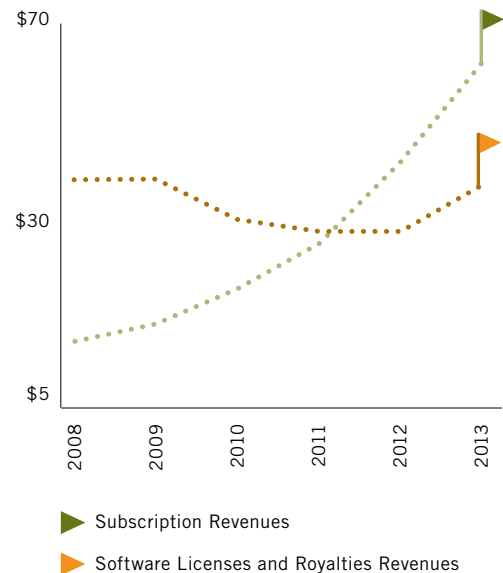
How is Tyler's e-filing business for courts progressing?

Since Tyler's acquisition of Wiznet in 2010, we have expanded our relationships with courts across the nation to establish Tyler as a leader in providing electronic filing solutions for courts. Our Odyssey File & Serve solution allows attorneys to file documents electronically with the courts, and the courts to serve documents electronically on parties involved in cases. We generally provide the e-filing solution with no up-front or ongoing out-of-pocket costs to the courts, and earn recurring revenues from fees paid by parties filing documents. Our e-filing revenues from courts increased 84 percent in 2013 to \$10.9 million.

We are actively pursuing new e-filing arrangements with existing and new Odyssey courts software clients, as well as with courts that do not use our case management software. The majority of courts in the country do not currently mandate e-filing, so the growth opportunity in this space is significant, although new e-filing contracts typically have long lead times before becoming mandatory.

During 2013, we signed 24 new e-filing contracts, including the Idaho State Judiciary, the Rhode Island Judiciary, and the Third Judicial Circuit of Michigan.

Transition to Cloud-Based Services in millions



APPRAISAL & TAX

Tyler expanded our appraisal and tax software line with a number of releases in 2013, including the iasWorld® Field Mobile feature. We also enhanced our iasWorld appraisal tax administration software with expanded cross-browser support, integration points and feature updates.

Contract highlights included an \$18 million iasWorld property tax solution for New York City, New York; contracts totaling \$2.8 million for iasWorld and Tyler Verify with Franklin County (Columbus), Ohio; and a \$7 million appraisal services agreement with Washington County, Pennsylvania. We also signed our first Tyler Verify contract in the state of Indiana with Vanderburgh County and expanded our international presence with an iasWorld software contract in Brunei.

leading the industry

In 2013, Tyler's spending on product development was at a record high level. Both new and existing clients benefit from Tyler's evergreen solutions, which include perpetual upgrades.

What is the status of the eFileTexas.gov engagement?

On January 1, 2014, Texas implemented mandatory electronic filing requirements for civil cases in the state's 10 largest counties and appellate courts, with the remaining courts to be added on a rolling schedule by 2016. As the statewide provider for mandatory electronic filing of civil court documents in Texas under a contract executed in 2012, Tyler orchestrated a successful rollout of the eFileTexas.gov site that began in June 2013 when Gregg County went live on the system. An estimated 90,000 attorneys will eventually be using the system for filing documents with courts in all 254 Texas counties.

In 2014, eFileTexas.gov is expected to handle 3.5 million electronic court filings — one of the largest statewide systems in the nation. We expect eFileTexas.gov to provide a powerful stream of recurring



revenues with attractive margins. Revenues from e-filing in Texas courts are expected to total approximately \$17 million in 2014, increasing to more than \$19 million annually in subsequent years. In 2013, however, we expensed approximately \$3.3 million of costs associated with the startup of the system, with revenues of approximately \$3.8 million in the second half of the year.

How does the eFileTexas.gov revenue arrangement differ from Tyler's other e-filing revenues?

We restructured our e-filing fee arrangement with the state of Texas in 2013 from a per-filing, transaction-based model to a fixed-fee arrangement. Filers now pay the courts a one-time e-filing fee when a case is initiated, and Tyler receives a fixed fee each quarter. The four-year contract is valued at approximately \$72 million. At December 31, 2013, our backlog included approximately \$68 million related to eFileTexas.gov. With our other

e-filing contracts, we generally collect a fee per filing, and because they are transaction-based, they are not included in backlog.

In 2012, you had an unprecedented opportunity to establish a presence in California courts with your Odyssey case management solution. What progress did Tyler make with that opportunity during 2013?

In early 2012, the state of California terminated a 10-year project with a systems integrator for developing a custom statewide case management system for the courts in the state's 58 counties, which unleashed demand for new systems for courts software in the nation's most populous state. With the clear leadership position our Odyssey solution has built in the case management space nationwide, we were confident that Tyler was well-positioned to compete in the California market. In 2013, we built on our early wins in California with further success in the state.



RECORDS & DOCUMENTS

Tyler's records and documents solutions facilitate public access and vital records management. As an example, Tyler's Eagle Recorder and Eagle Web with Fraud Guard offer a secure, Web-accessible solution and give residents the flexibility to conduct online record searches and register to be alerted when a document with their name is recorded.

Contract highlights included an Eagle Recorder software contract including both licenses and SaaS solutions with Wayne County (Detroit), Michigan; as well as Eagle contracts with Riverside County, California; and Palm Beach County, Florida.

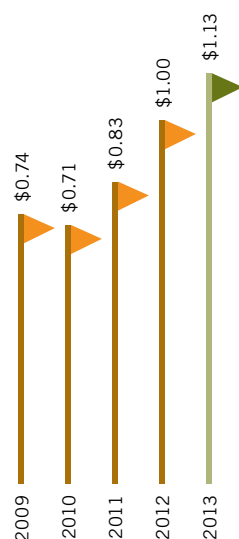
2013 Quarterly Earnings Per Share

in dollars



Annual Earnings Per Share

in dollars



Tyler was one of three providers selected to enter into master service agreements that allow counties to bypass the requirement to issue individual requests for proposal to purchase new systems. We signed contracts during 2013 with courts in 11 counties in California, including Orange, Fresno and Merced. Six Northern California counties came together to form the NorCal Collaboration Project, an innovative arrangement under which they each signed five-year SaaS contracts to jointly implement Odyssey in a single project. To date, 12 of the 14 California counties that have signed contracts for new courts systems since 2012 have selected Tyler's Odyssey solution, with seven of them choosing our SaaS model. The market in California remains very active, and we anticipate that courts in some of the state's larger counties will make decisions during 2014 to replace their aging case management systems.

Our success in California courts has not been limited to sales, however. In January 2014, our first California courts client, San Luis Obispo County, went live on Odyssey, just 13 months after we kicked off the implementation.

How is Tyler building on its leadership position in financial software for local governments and schools?

While we are excited about the potential of our e-filing and case management solutions, our financial product suites — Munis and Incode — form our foundation. These products accounted for approximately one-half of our revenues and an even greater percentage of our operating profit in 2013. Our core financial solutions achieved higher win rates against key competitors during the past year, while continuing to expand our presence in larger cities, counties and school districts.

The addition of EnerGov, the planning, permitting, licensing, and land management solution we acquired late in 2012, also added to solid double-digit growth in our financial systems revenues in 2013. EnerGov contributed wins in both standalone licensing and permitting opportunities and in contracts that also included our Munis or Incode financial solutions.



PLANNING, PERMITTING & LICENSING

Since acquiring EnerGov in November 2012, Tyler has had several major wins over our largest competitor for that product suite, including contracts in 2013 with Temecula, California; Palm Beach County, Florida; and Columbia, Missouri. Other key EnerGov contracts included the Washington Suburban Sanitation Commission and the city of Richmond Hill, Canada, as well as San Mateo and Tulare counties in California.

What is the status of Microsoft Dynamics AX, the financial product you jointly developed for the public sector with Microsoft?

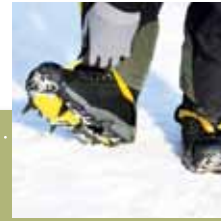
Dynamics AX 2012 was released by Microsoft in late 2011. We have two revenue streams related to this product, which we jointly developed by adding public sector functionality to the Microsoft product. We sell this product to targeted public sector entities through our direct sales channel, and we receive royalties on both licenses and maintenance from public sector sales by other Microsoft partners worldwide.

Although 2013 was only the second year in which we received royalties from Microsoft, they grew to \$3.1 million from \$756,000 in 2012. In the first two years, Dynamics AX has gained broad geographic penetration with diverse public sector entities worldwide, with royalties in 2013 from public sector sales in 38 countries. This relationship allows Tyler to bring our deep public sector expertise to clients all over the world through the Microsoft channel and to generate revenues in markets we wouldn't have otherwise pursued on a direct basis — such as organizations in Zimbabwe, Poland and India. We expect that Dynamics AX sales through Microsoft's partner network will continue to expand and that royalties will become more meaningful in future years as the product continues to gain traction.

Tyler's direct sales of Microsoft Dynamics AX in 2013 included contracts with Columbus, Ohio, the nation's 15th-largest city; all 77 district courts of the Supreme Court of Oklahoma; Walker County, Texas; and the Maricopa Association of Governments in Phoenix, Arizona. Tyler was also recognized as the 2013 United States Microsoft Dynamics Public Sector Partner of the Year.

You've won an increasing number of large deals in recent years. Why is that, and does it have any bearing on your relationships with small and mid-size clients?

Historically, many of the nation's largest public sector organizations tended to defer to a select few large multinational providers when choosing a technology partner. These providers were often chosen based on their name recognition and horizontal capabilities, even though their vertical expertise in the public sector may



Expanding our presence in the California courts market

When the state of California abandoned a 10-year effort to develop a custom statewide case management system, Tyler's clear position of national leadership in the courts software market enabled us to achieve early success in that state. Today, our Odyssey® court case management system has been selected by courts throughout the state to manage their growing case activity more effectively and do more with less.



PUBLIC SAFETY

Tyler's public safety solutions grew at a steady pace, with a 14 percent increase in our client base from 2012 to 2013. The largest contract was with the city of Tupelo, Mississippi, a combined agreement with Tyler's Incode court solution. Other significant contracts were the Bowie County-Texarkana Communication Center in Texas and Coahoma County, Mississippi.

visible results

Tyler's Versatrans product increased its GPS market share by 600 in-vehicle devices through contracts with Shelby County and Washington Consolidated School District, Tennessee; Dubuque Community School District, Iowa; and Shenendehowa PSD, New York.



STUDENT MANAGEMENT

Tyler continued to enhance our student management offerings in 2013 with the release of Traversa®, a Web-based K-12 transportation management solution, as well as the launch of a new Tyler Telematic GPS device with advanced data collection capabilities for our Versatrans product. In addition, Tyler has been named a preferred vendor in Oklahoma, allowing school districts to bypass individual RFPs and purchase Tyler SIS at a negotiated rate.

Contract highlights include a Versatrans deal with Brownsville ISD, Texas — our largest Versatrans sale to date; and the sale of 442 additional Tyler Telematic GPS units to the Polk County School District, Florida — making it the largest Tyler Telematic GPS fleet at 691 buses.

have been lacking. Meanwhile, Tyler continued to build our business consistently, staying true to our exclusive focus on solutions for public sector clients and devoting all of our investments to innovations that address their unique needs. Today, Tyler Technologies is recognized by public sector entities of all sizes for its resources, financial strength and vertical expertise.

What product enhancements and new releases did Tyler announce in 2013?

We continued to refine many of our existing products by enhancing features, functionality and technology. New releases included Traversa, a comprehensive Web-based school transportation management solution for K-12; the iasWorld Field Mobile feature; CAFR Statement Builder for the software suites of Eden, FundBalance, Incode and Munis; and Tyler eTimekeeper, a Web-based time and attendance tracker that can be used with mobile devices as well as desktop computers.

How do mobile technologies fit into your product development strategy?

Every new Tyler solution or product enhancement is driven by the needs of our clients — and mobile solutions are no exception. Mobile apps and utilities make it possible for employees in the field to efficiently gather and securely share information with the main office or other authorized parties in real time. We know from experience that every dollar spent by schools and governments has to justify its worth, and mobile solutions offer a level of flexibility and responsiveness that makes them a good fit for the public sector. We will continue to develop and refine products that extend our clients' capabilities and enhance the user experience, including mobile apps, cloud-based solutions and traditional licensed products.

What mobile solutions does Tyler currently offer?

Tyler has already developed and released a number of mobile solutions that enable our clients to do their jobs more effectively and more efficiently. Our EnerGov Mobile App Suite features Apple iPad® functionality that allows code enforcement officers, inspectors and other agency workers to make notes and take photos on site, manage workflow productivity, and update information in real time via Wi-Fi connectivity. We also offer the Incode Mobile Management Console for Windows 8 and Windows RT, which offers remote tablet access to financial and personnel information through available 3G, 4G or Wi-Fi networks. Other mobile solutions from Tyler include Munis My Work for approvals, notifications and alerts; the Tyler Public Safety mobile app for real-time information at the scene; and the Traversa, iasWorld Field Mobile, and Tyler eTimekeeper solutions previously mentioned.

What recognition for its success did Tyler receive during 2013?

Every business decision we make is driven by our commitment to serving the public sector. For that reason, we value the recognition we receive from respected sources

in the business world — because each award and accolade serves to reinforce the value we deliver to our clients.

We achieved our highest ranking yet on the *Forbes* list of 100 Best Small Companies in America, having been named to the list for six of the last seven years. Our 2013 ranking was 25th — 11 spots higher than the previous year. Criteria included companies with revenues from \$5 million to \$1 billion, a share price above \$5, a healthy return on equity, sustained sales and earnings growth in the past 12 months and over the last five years, and solid stock performance in comparison to industry peers.

For the sixth consecutive year, Tyler appeared on the Software 500 ranking, published by *Software Magazine*. The Software 500 is based on revenue from software licenses, maintenance and support, training, and software-related services and consulting. Tyler ranked 166 on the 2013 list, which was based on software and services revenue for 2012.

We also made our fourth appearance on the Barron's 400 Index. The index uses proprietary methodologies to identify 400 publicly traded companies it considers to be financially sound, and only around 6 percent of all publicly listed North American companies are selected. The Barron's 400 Index has outperformed the broader U.S. equity market by more than 5 percentage points per year in the last decade.

Tyler is proud of the hard work and public sector expertise that these awards represent, and we will continue to challenge our team to further extend our position as an industry innovator and leader.

The preceding Q&A is a composite representation of the views of Tyler management with regard to company performance and market perspectives. For further information, visit tylertech.com or contact our investor relations team at info@tylertech.com.



SCHOOL FINANCIAL

In keeping with the growing popularity of SaaS solutions, many of our existing clients made the transition from traditional licenses to SaaS in 2013. Tyler's SaaS solutions also attracted several new clients to our School Financial solutions, while sales of traditional licenses remained strong.

School Financial contract highlights for 2013 included Munis contracts with the Lewisville Independent School District in Texas and the Santa Barbara Unified School District in California.

2013

financial
information



Empowering people who serve the public®

Stock Market Data

Our common stock is traded on the New York Stock Exchange under the symbol "TYL." At December 31, 2013, we had approximately 1,776 stockholders of record. A number of our stockholders hold their shares in street name; therefore, there are substantially more than 1,776 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
2012: First Quarter	\$ 39.43	\$ 29.67
Second Quarter	41.61	36.00
Third Quarter	44.41	36.99
Fourth Quarter	49.60	41.95
2013: First Quarter	\$ 61.60	\$ 48.86
Second Quarter	70.49	57.00
Third Quarter	88.68	68.60
Fourth Quarter	105.74	83.25

We did not pay any cash dividends in 2013 or 2012. 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.

As of December 31, 2013, we had authorization to repurchase up to 1.7 million additional shares of Tyler common stock. There was no repurchase activity during the twelve months ended December 31, 2013. The repurchase program, which was approved by our board of directors, was announced in October 2002, and was amended in April 2003, July 2003, October 2004, October 2005, May 2007, May 2008, October 2008, May 2009, July 2010, October 2010 and September 2011. There is no expiration date specified for the authorization and we intend to repurchase stock under the plan from time to time.

Selected Financial Data

SELECTED FINANCIAL DATA

	For the Years Ended December 31,				
(In thousands, except per share data)	2013	2012	2011	2010	2009
STATEMENT OF OPERATIONS DATA:					
Revenues	\$416,643	\$363,304	\$309,391	\$288,628	\$290,286
Costs and expenses:					
Cost of revenues	223,440	195,602	167,479	160,311	161,523
Selling, general and administrative expenses	98,289	86,706	75,650	69,480	70,115
Research and development expense	23,269	20,140	16,414	13,971	11,159
Amortization of customer and trade name intangibles	4,517	4,279	3,331	3,225	2,705
Operating income	67,128	56,577	46,517	41,641	44,784
Other expense, net	(1,309)	(2,709)	(2,404)	(1,742)	(146)
Income from operations before income taxes	65,819	53,868	44,113	39,899	44,638
Income tax provision	26,718	20,874	16,556	14,845	17,628
Net income	\$ 39,101	\$ 32,994	\$ 27,557	\$ 25,054	\$ 27,010
Net income per diluted share	\$ 1.13	\$ 1.00	\$ 0.83	\$ 0.71	\$ 0.74
Weighted average diluted shares	34,590	32,916	33,154	35,528	36,624
STATEMENT OF CASH FLOWS DATA:					
Cash flows provided by operating activities	\$ 66,090	\$ 58,668	\$ 56,435	\$ 35,350	\$ 42,941
Cash flows used by investing activities	(25,658)	(34,736)	(28,809)	(8,694)	(13,658)
Cash flows provided (used) by financing activities	32,038	(18,852)	(28,414)	(34,238)	(21,349)
BALANCE SHEET DATA:					
Total assets	\$444,488	\$338,666	\$295,391	\$264,032	\$270,670
Revolving line of credit	—	18,000	60,700	26,500	—
Shareholders' equity	246,319	145,299	78,110	106,972	134,358

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

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. These 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 opinion only as of the date hereof. We undertake no obligation to revise or publicly release the results of any revisions to these forward-looking statements. Readers should carefully review the risk factors described in documents we file from time to time with the Securities and Exchange Commission.

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 other similar words or 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 software as a service ("SaaS"), which utilizes the Tyler private cloud, and electronic document filing solutions ("e-filing"). In 2010 we began providing e-filing for courts and law offices, which simplify the filing and management of court related documents. Revenues for e-filing are derived from transaction fees and in some cases fixed fee arrangements. We also provide property appraisal outsourcing services for taxing jurisdictions.

Our products generally automate three major functional areas: (1) financial management and education, (2) courts and justice and (3) property appraisal and tax and we report our results in two segments. The Enterprise Software Solutions ("ESS") segment provides municipal and county governments and schools with software systems and services 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 ("ATSS") 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 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 and royalties; subscription-based arrangements; software services; maintenance and appraisal services. Subscriptions and maintenance are considered recurring revenue sources and comprised approximately 61% of our revenue in 2013. The number of new SaaS customers and the number of existing customers who convert from our traditional software arrangements to our SaaS model are a significant driver to our business, together with new software license sales and maintenance rate increases. In addition, we also monitor our customer base and churn as we historically have experienced very low customer turnover. During 2013, our customer turnover was approximately 2%.

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

- **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 and royalties, subscription-based services, and maintenance and support. Our appraisal projects are cyclical 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, 2013, our total employee count increased to 2,573 from 2,388 at December 31, 2012.
- **Selling, General and Administrative (“SG&A”) Expenses** – The primary components of SG&A expenses are administrative and sales personnel salaries and commissions, share-based compensation expense, marketing expense, rent and professional fees. Sales commissions typically fluctuate with revenues and share-based compensation expense generally increases when the market price of our stock increases. 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 discretionary purchases of treasury stock. During 2013, we invested \$26.9 million in property and equipment. Our investment in property and equipment included \$20.3 million in connection with the construction of an office building in Plano, Texas. 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.

Outlook

We expect the trend of gradual improvements in the marketplace to continue in 2014. We have made significant investments in our business that we believe will enhance our market leadership and improve long-term revenue and margin growth.

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 proportional 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 and royalties, subscription-based services, appraisal services, maintenance and support, and

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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 creating additional custom reports. 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 proportional 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 value of products delivered and services performed in the event of an early termination.

For SaaS arrangements, we evaluate whether the customer has the contractual right to take possession of our software at any time during the hosting period without significant penalty and whether the customer can feasibly maintain the software on the customer's hardware or enter into another arrangement with a third party to host the software. 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. For SaaS arrangements that do not meet the criteria for recognition under ASC 985-605, we account for the elements under ASC 605-25, Multiple Element Arrangements using all applicable facts and circumstances, including whether (i) the element has stand-alone value, (ii) there is a general right of return and (iii) the revenue is contingent on delivery of other elements. We allocate the contract value to each element of the arrangement that qualifies for treatment as a separate element based on vendor-specific objective evidence of fair value ("VSOE"), and if VSOE is not available, third party evidence, and if third party evidence is unavailable, estimated selling price. For professional services associated with SaaS arrangements that we determine do not have stand-alone value to the customer or are contingent on delivery of other elements, 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.

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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. We review 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. These intangible assets (other than goodwill) are amortized over their estimated useful lives. We currently have no intangible assets with indefinite lives other than goodwill.

When testing goodwill for impairment quantitatively, we first compare the fair value of each reporting unit with its carrying amount. If the carrying amount of a reporting unit exceeds its fair value, a second step is performed to measure the amount of potential impairment. In the second step, we compare the implied fair value of reporting unit goodwill with the carrying amount of the reporting unit's goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized. The fair values calculated in our impairment tests are determined using discounted cash flow models involving several assumptions. The assumptions that are used are based upon what we believe a hypothetical marketplace participant would use in estimating fair value. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain. 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.

Our annual goodwill impairment analysis, which we performed quantitatively during the second quarter of 2013, did not result in an impairment charge. During 2013, we did not identify any triggering events which would require an update to our annual impairment review.

All intangible assets (other than goodwill) are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of other intangible assets is 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.

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

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

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 weighted-average period the stock options are expected to be outstanding based primarily on the options' vesting terms, remaining contractual life and the employees' expected exercise based on historical patterns. 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, 2013, 2012 and 2011.

Years ended December 31,	Percentage of Total Revenue		
	2013	2012	2011
Revenue:			
Software licenses and royalties	9.8%	9.3%	10.5%
Subscriptions	14.8	12.3	10.1
Software services	22.4	23.0	22.5
Maintenance	46.0	47.3	47.4
Appraisal services	5.0	6.2	7.5
Hardware and other	2.0	1.9	2.0
Total revenue	100.0	100.0	100.0
Operating Expenses:			
Cost of software licenses, royalties and acquired software	1.1	1.1	1.3
Cost of software services, maintenance and subscriptions	47.9	47.2	46.5
Cost of appraisal services	3.3	4.1	4.7
Cost of hardware and other	1.3	1.4	1.6
Selling, general and administrative expenses	23.6	23.9	24.5
Research and development expense	5.6	5.5	5.3
Amortization of customer base and trade name intangibles	1.1	1.2	1.1
Operating income	16.1	15.6	15.0
Other expense	0.3	0.8	0.7
Income before income taxes	15.8	14.8	14.3
Income tax provision	6.4	5.7	5.4
Net income	9.4%	9.1%	8.9%

2013 Compared to 2012

Revenues

Software licenses and royalties.

The following table sets forth a comparison of our software licenses and royalties revenues for the years ended December 31:

(\$ in thousands)	2013	2012	Change	
			\$	%
ESS	\$38,774	\$32,060	\$6,714	21%
ATSS	2,067	1,868	199	11
Total software licenses and royalties revenue	\$40,841	\$33,928	\$6,913	20%

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Since March 2012, we have acquired two companies which provide financial and human capital management software solutions to the K-12 education market and one company that provides enterprise permitting, land management, licensing and regulatory software solutions to governmental agencies. The results of these acquisitions are included in our ESS segment from the dates of their acquisitions. Excluding the impact of acquisitions, total software licenses and royalties revenue increased 12% compared to 2012. Approximately half of the growth was due to an increase of \$2.3 million in royalties on sales of Microsoft Dynamics AX by other Microsoft partners compared to the prior year. We record royalty revenue when the fees are fixed or determinable, which is known when we receive notice of the amounts earned pursuant to our royalty arrangements which are generally 30 to 60 days after each quarterly reporting period. Royalty revenue is dependent upon sales volume from Microsoft partners, as well as the timing of maintenance renewals, and can vary substantially from period to period. Excluding the impact of acquisitions, software licenses grew 5% mainly due to increased investments in product development over the past few years. However, software license growth was reduced somewhat because of a growing number of customers choosing our subscription-based options, rather than purchasing the software under a traditional perpetual software license arrangement. Subscription-based arrangements result in no software license revenues in the initial year as compared to traditional perpetual software license arrangements but generate higher overall subscription-based services revenue over the term of the contract. We had 100 new customers that entered into subscription-based arrangements in 2013 compared to 76 new customers in 2012.

Subscriptions.

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

(\$ in thousands)	2013	2012	Change	
			\$	%
ESS	\$59,070	\$43,319	\$15,751	36%
ATSS	2,794	1,299	1,495	115
Total subscriptions revenue	\$61,864	\$44,618	\$17,246	39%

Subscription-based services revenue primarily consists of revenues derived from our SaaS arrangements, which utilize the Tyler private cloud. As part of our subscription-based services, we also provide e-filing that simplify the filing and management of court related documents for courts and law offices. Revenues for e-filing are derived from transaction fees or in some cases fixed fee arrangements. The contract term for SaaS arrangements range from one to 10 years but are typically for a period of three to six years.

Excluding the impact of acquisitions, subscription-based services revenue increased 37% compared to 2012. New SaaS customers as well as existing customers who converted to our SaaS model provided the majority of the subscription-based revenue increase. In 2013, we added 100 new customers and 63 existing customers elected to convert to our SaaS model. E-filing services also contributed approximately \$5.0 million of the subscription revenue increase. E-filing revenue included \$3.8 million related to a new contract with the Texas Office of Court Administration for our Odyssey File and Serve e-filing system for Texas courts ("e-File Texas.gov"), which was implemented in September 2013. This contract is a fixed fee arrangement and we expect it will provide a long-term recurring revenue stream of \$17 million to \$19 million annually when e-filing becomes mandatory in Texas in 2014. The remaining e-filing revenue increase is mainly the result of existing clients expanding mandatory e-filing for court documents.

Software services.

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

(\$ in thousands)	2013	2012	Change	
			\$	%
ESS	\$85,459	\$76,103	\$9,356	12%
ATSS	7,808	7,305	503	7
Total software services revenue	\$93,267	\$83,408	\$9,859	12%

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Software services revenues primarily consist of professional services billed in connection with the installation of our software, conversion of customer data, training customer personnel and consulting. New customers who purchase our proprietary software licenses generally also contract with us to provide for the related software services. Existing customers also periodically purchase additional training, consulting and minor programming services. Excluding the impact of acquisitions, software services increased 7% compared to 2012. The increase is partly due to growth in software license activity and due to contract arrangements that included more programming and other services.

Maintenance.

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

(\$ in thousands)	2013	2012	Change	
			\$	%
ESS	\$175,180	\$155,290	\$19,890	13%
ATSS	16,540	16,561	(21)	—
Total maintenance revenue	\$191,720	\$171,851	\$19,869	12%

We provide maintenance and support services for our software products and certain third party software. Excluding the impact of acquisitions, maintenance revenue grew 9% from 2012. This increase was due to growth in our installed customer base from new software license sales and maintenance rate increases.

Appraisal services.

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

(\$ in thousands)	2013	2012	Change	
			\$	%
ESS	\$ —	\$ —	\$ —	—%
ATSS	20,825	22,543	(1,718)	(8)
Total appraisal services revenue	\$20,825	\$22,543	\$(1,718)	(8)%

Appraisal services revenue declined 8% in 2013 compared to 2012. The appraisal services business is somewhat cyclical and driven in part by statutory revaluation cycles in various states. The decline is mainly due to the completion in mid-2012 of a large contract in Pennsylvania. We expect appraisal revenues for 2014 will increase slightly compared to 2013.

Cost of Revenues and Gross Margins

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

(\$ in thousands)	2013	2012	Change	
			\$	%
Software licenses and royalties	\$ 2,377	\$ 1,983	\$ 394	20%
Acquired software	2,078	1,888	190	10
Software services, maintenance and subscriptions	199,617	171,584	28,033	16
Appraisal services	13,809	14,889	(1,080)	(7)
Hardware and other	5,559	5,258	301	6
Total cost of revenues	\$223,440	\$195,602	\$27,838	14%

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

Gross margin percentage	2013	2012	Change
Software licenses, royalties and acquired software	89.1%	88.6%	0.5%
Software services, maintenance and subscriptions	42.4	42.8	(0.4)
Appraisal services	33.7	34.0	(0.3)
Hardware and other	31.6	24.4	7.2
Overall gross margin	46.4%	46.2%	0.2%

Software licenses, royalties and acquired software. Costs of software licenses, royalties and acquired software are primarily comprised of third party software costs and amortization expense for software acquired through acquisitions. We do not have any direct costs associated with royalties. In 2013, our software licenses, royalties and acquired software gross margin percentage increased compared to 2012 mainly due to higher revenues from royalties. The margin also benefited from a product mix that included slightly more proprietary software revenues, which have a higher gross margin than third party software.

Software services, maintenance and subscription-based services. Cost of software services, maintenance and subscription-based services 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 SaaS arrangements and e-filing. Maintenance and various other services such as SaaS 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. However, we accelerated hiring in 2013 to ensure that we were well-positioned to deliver our current backlog and anticipated new business. In late 2012, we signed a contract with the Texas Office of Court Administration for e-FileTexas.gov to manage e-filing of court documents. In early 2013, the state of Texas issued an order mandating e-filing in civil cases beginning in January 2014. Mandatory e-filing will be phased in over a two and a half year period, beginning with the largest counties in January 2014. We will be paid on a fixed fee basis but had very limited revenues in 2013 from e-FileTexas.gov. However, during 2013, we incurred expenses of approximately \$3.3 million in connection with implementing the system in courts across the state. Excluding the limited revenues and cost incurred in connection with implementing e-FileTexas.gov in 2013, our software services, maintenance and subscription services gross margin would have been approximately 42.8%. Our implementation and support staff has increased by 202 employees since 2012. Most of these additions occurred mid-to late 2013.

Appraisal services. Appraisal services revenues are approximately 5% of total revenues. The appraisal services gross margin declined slightly compared to 2012. 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 2013 increased 0.2% from 2012. The increase was due to higher royalty revenue and also benefited from a product mix that included slightly higher proprietary software revenues than third party software. Costs incurred related to our implementation of e-FileTexas.gov with minimal related revenues as well as increased hiring of implementation and support staff in order to expand our capacity to implement our contract backlog offset some of the positive impact of higher royalty and proprietary software revenue.

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:

(\$ in thousands)	2013	2012	Change	
			\$	%
Selling, general and administrative expenses	\$98,289	\$86,706	\$11,583	13%

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SG&A as a percentage of revenues was 23.6% in 2013 compared to 23.9% in 2012. Excluding costs from acquisitions, almost half of the SG&A expense increase is due to increased stock compensation expense resulting from the substantial increase in our stock price over the last twelve months and higher payroll taxes associated with increased stock option exercise activity. Commission expense has also increased compared to the prior year periods due to higher sales.

Research and Development Expense

Research and development expense consists primarily of salaries, employee benefits and related overhead costs associated with product development. The following table sets forth a comparison of our research and development expense for the years ended December 31:

(\$ in thousands)	2013	2012	Change	
			\$	%
Research and development expense	\$23,269	\$20,140	\$3,129	16%

Research and development expense consist mainly of costs associated with development of new products and new software platforms from which we do not currently generate revenue. These include the next version of Microsoft Dynamics AX project, as well as other new product development efforts. In 2007, we entered into a Software Development and License Agreement, which provides 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. This agreement and subsequent amendments granted Microsoft intellectual property rights in 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 and royalties on direct and indirect public-sector sales worldwide of the solutions co-developed under this arrangement. In addition, Tyler has agreed to commit certain resources to the development of the next version of Dynamics AX and will receive software and maintenance royalties on direct and indirect public-sector sales worldwide of the solutions co-developed under this arrangement.

Our research and development expense increased \$3.1 million in 2013 compared to 2012. In 2013 we did not have any research and development expense offsets earned under the terms of our agreement with Microsoft compared to \$1.0 million in research and development expense offsets in 2012.

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 operating expense. The estimated useful lives of both customer and trade name intangibles are five to 25 years. The following table sets forth a comparison of amortization of customer and trade name intangibles for the years ended December 31:

(\$ in thousands)	2013	2012	Change	
			\$	%
Amortization of customer and trade name intangibles	\$4,517	\$4,279	\$238	6%

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):

2014	\$ 4,515
2015	4,515
2016	4,515
2017	4,515
2018	4,366

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

Other

The following table sets forth a comparison of other expense, net for the years ended December 31:

(\$ in thousands)	2013	2012	Change	
			\$	%
Other expense, net	\$1,309	\$2,709	\$(1,400)	(52)%

Other expense is primarily comprised of interest expense, non-usage and other fees associated with our revolving line of credit agreement. Interest expense was lower in 2013 than 2012 because we maintained higher debt levels in 2012 associated primarily with several acquisitions completed from October 2011 through November 2012.

Income Tax Provision

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

(\$ in thousands)	2013	2012	Change	
			\$	%
Income tax provision	\$26,718	\$20,874	\$5,844	28%
Effective income tax rate	40.6%	38.8%		

The effective income tax rates 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, disqualifying incentive stock option dispositions and non-deductible meals and entertainment costs. We experienced significant stock option exercise activity in 2013 that generated \$28.2 million excess tax benefits. Excess tax benefits reduce tax payments but do not significantly reduce the effective tax rate and can result in limitations on other deductions. In 2013, limitations resulting from excess tax benefits eliminated the qualified manufacturing activities deduction, which negatively impacted our effective tax rate.

2012 COMPARED TO 2011

Revenues

Software licenses and royalties.

The following table sets forth a comparison of our software licenses and royalties revenues for the years ended December 31:

(\$ in thousands)	2012	2011	Change	
			\$	%
ESS	\$32,060	\$30,194	\$1,866	6%
ATSS	1,868	2,400	(532)	(22)
Total software licenses and royalties revenue	\$33,928	\$32,594	\$1,334	4%

Excluding the impact of acquisitions, total software licenses and royalties revenue declined by 3% compared to 2011. Most of the decline was due to fewer add-on sales to our existing customer base. In addition, software license growth was reduced somewhat because of a growing number of customers choosing our subscription-based options, rather than purchasing the software under a traditional perpetual software license arrangement. Subscription-based arrangements result in no software license revenues in the initial year as compared to traditional perpetual software license arrangements but generate higher overall subscription-based services revenue over the term of the contract. We had 76 new customers that entered into subscription-based arrangements in 2012 compared to 47 new customers in 2011.

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

Subscriptions.

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

(\$ in thousands)	2012	2011	Change	
			\$	%
ESS	\$43,319	\$30,400	\$12,919	42%
ATSS	1,299	760	539	71
Total subscriptions revenue	\$44,618	\$31,160	\$13,458	43%

Excluding the impact of acquisitions, subscription-based services revenue increased 40% compared to 2011. New SaaS customers as well as existing customers who converted to our SaaS model provided the majority of the subscription-based revenue increase. In 2012, we added 76 new customers and 68 existing customers elected to convert to our SaaS model. E-filing services also contributed approximately \$2.3 million of the subscription revenue increase as a result of new clients implementing e-filing and several existing clients adopting or expanding mandatory e-filing for court documents in the last half of 2011 and 2012.

Software services.

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

(\$ in thousands)	2012	2011	Change	
			\$	%
ESS	\$76,103	\$60,840	\$15,263	25%
ATSS	7,305	8,777	(1,472)	(17)
Total software services revenue	\$83,408	\$69,617	\$13,791	20%

Excluding the impact of acquisitions, software services increased 14% compared to 2011. The increase is due partly to contract arrangements that included more programming services as well as several state-wide arrangements that in addition to services, include more third party vendor services to build certain software interfaces.

Maintenance.

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

(\$ in thousands)	2012	2011	Change	
			\$	%
ESS	\$155,290	\$130,999	\$24,291	19%
ATSS	16,561	15,499	1,062	7
Total maintenance revenue	\$171,851	\$146,498	\$25,353	17%

Excluding the impact of acquisitions, maintenance revenue grew 9% from 2011. This increase was due to growth in our installed customer base and maintenance rate increases on most of our product lines.

Appraisal services.

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

(\$ in thousands)	2012	2011	Change	
			\$	%
ESS	\$ —	\$ —	\$ —	—%
ATSS	22,543	23,228	(685)	(3)
Total appraisal services revenue	\$22,543	\$23,228	\$(685)	(3)%

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

Appraisal services revenue declined 3% in 2012 compared to 2011. The appraisal services business is somewhat cyclical and driven in part by statutory revaluation cycles in various states. The decline is mainly due to the completion in mid-2012, of a large contract in Pennsylvania offset slightly by the start-up of smaller projects, including several in Ohio.

Cost of Revenues and Gross Margins

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

(\$ in thousands)	2012	2011	Change	
			\$	%
Software licenses and royalties	\$ 1,983	\$ 3,034	\$ (1,051)	(35)%
Acquired software	1,888	1,125	763	68
Software services, maintenance and subscriptions	171,584	143,776	27,808	19
Appraisal services	14,889	14,550	339	2
Hardware and other	5,258	4,994	264	5
Total cost of revenues	\$195,602	\$167,479	\$28,123	17%

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

Gross margin percentage	2012	2011	Change
Software licenses, royalties and acquired software	88.6%	87.2%	1.4%
Software services, maintenance and subscriptions	42.8	41.9	0.9
Appraisal services	34.0	37.4	(3.4)
Hardware and other	24.4	20.7	3.7
Overall gross margin	46.2%	45.9%	0.3%

Software licenses, royalties and acquired software. In 2012, our software license gross margin percentage increased compared to 2011 due to higher royalties and because our product mix included less third party software which offset higher amortization expense associated with acquisitions.

Software services, maintenance and subscription-based services. In 2012, the software services, maintenance and subscriptions gross margin increased compared to the prior year partly because we improved our utilization of our support and maintenance staff and due to annual rate increases on certain services. Excluding 147 employees added with acquisitions, our implementation and support staff has increased by 103 employees since 2011. Most of these additions occurred mid-to late 2012.

Appraisal services. Appraisal services revenues are approximately 6% of total revenues. The appraisal services gross margin declined compared to 2011. The appraisal services gross margin in 2011 was also favorably impacted by operational efficiencies associated with a large revaluation contract, which began in mid-2010 and was substantially complete by mid-2011.

Our blended gross margin for 2012 increased 0.3% from 2011 mainly due to leverage in the utilization of our support, maintenance and subscription-based services staff and economies of scale and slightly higher rates on certain services. The gross margin also benefited from lower third party software costs and higher royalties.

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

Selling, General and Administrative Expenses

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

(\$ in thousands)	2012	2011	Change	
			\$	%
Selling, general and administrative expenses	\$86,706	\$75,650	\$11,056	15%

Excluding the impact of acquisitions, SG&A increased approximately 11% compared to 2011. SG&A as a percentage of revenues was 23.9% in 2012 compared to 24.5% in 2011. SG&A expenses increased due to higher commission expense in connection with increased sales; increased headcount in sales and related expenses to support geographic expansion; and increased incentive compensation costs due to improved results and higher stock compensation expense because our company stock price has increased substantially over the last few years.

Research and Development Expense

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

(\$ in thousands)	2012	2011	Change	
			\$	%
Research and development expense	\$20,140	\$16,414	\$3,726	23%

Our research and development expense increased \$3.7 million in 2012 compared to 2011. The increase is mainly due to lower reimbursements from Microsoft in 2012. In 2012, we had \$1.0 million in research and development expense offsets compared to \$3.5 million in 2011, which were the amounts earned under the terms of our agreement with Microsoft. Under our amended agreement with Microsoft, the project included offsets to research and development expense, varying in amount from quarter to quarter from 2009 through 2012 for a total of approximately \$6.2 million. As of September 30, 2012, we received the final \$1.0 million under the agreement.

Amortization of Customer and Trade Name Intangibles

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

(\$ in thousands)	2012	2011	Change	
			\$	%
Amortization of customer and trade name intangibles	\$4,279	\$3,331	\$948	28%

In 2012, we completed four acquisitions that increased amortizable customer and trade name intangibles by approximately \$11.1 million. This amount is being amortized over a weighted average period of 11.8 years.

Other

The following table sets forth a comparison of other expense, net for the years ended December 31:

(\$ in thousands)	2012	2011	Change	
			\$	%
Other expense, net	\$2,709	\$2,404	\$305	13%

Interest expense was higher in 2012 than 2011 due to higher debt levels associated with several acquisitions completed since October 2011 and stock repurchases in the last half of 2011. The effective interest rate in 2012 was 3.4% compared to 3.3% in 2011.

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

Income Tax Provision

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

(\$ in thousands)	2012	2011	Change	
			\$	%
Income tax provision	\$20,874	\$16,556	\$4,318	26%
Effective income tax rate	38.8%	37.5%		

The effective income tax rates 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, disqualifying incentive stock option dispositions and non-deductible meals and entertainment costs. The effective income tax rate in 2011 was also reduced by a research and development tax credit. The qualified manufacturing activities deduction declined in 2012 contributing to a higher effective tax rate.

FINANCIAL CONDITION AND LIQUIDITY

As of December 31, 2013, we had cash and cash equivalents of \$78.9 million and investments available-for-sale of \$1.3 million, compared to cash and cash equivalents of \$6.4 million and investments available-for-sale of \$2.0 million at December 31, 2012. As of December 31, 2013, we had no outstanding borrowings and an outstanding letter of credit totaling \$2.0 million. Some of our customers require a letter of credit in connection with our contracts. The notional amount of performance guarantees outstanding secured by letter of credit as of December 31, 2013 was estimated to be approximately \$29.0 million. We do not believe this letter of credit will be required to be drawn upon. We believe that cash from operating activities, cash on hand and access to the credit markets provides us with sufficient flexibility to meet our long-term financial needs.

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

(\$ in thousands)	2013	2012	2011
Cash flows provided (used) by:			
Operating activities	\$ 66,090	\$ 58,668	\$ 56,435
Investing activities	(25,658)	(34,736)	(28,809)
Financing activities	32,038	(18,852)	(28,414)
Net increase (decrease) in cash and cash equivalents	\$ 72,470	\$ 5,080	\$ (788)

Net cash provided by operating activities continues to be our primary source of funds to finance operating needs and capital expenditures. Other potential capital resources include cash on hand, public and private issuances of debt or equity securities, and bank borrowings. It is possible that our ability to access the capital and credit markets in the future may be limited by economic conditions or other factors. We currently believe that cash provided by operating activities, cash on hand and access to the credit markets are sufficient to fund our working capital requirements, capital expenditures, income tax obligations, and share repurchases for at least the next twelve months.

In 2013, operating activities provided net cash of \$66.1 million, primarily generated from net income of \$39.1 million, non-cash depreciation and amortization charges of \$13.8 million and non-cash share-based compensation expense of \$11.7 million. Cash from operations also benefited from timing of payments on wages and bonuses. In addition, deferred revenue balances were higher than 2012 due to an increase in annual software maintenance billings as a result of growth in our installed customer base and growth in subscription-based arrangements. These increases in liabilities were offset somewhat by higher accounts receivable balances from annual software maintenance billings, progress billings associated with large contracts and prepaid commissions on large contracts.

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.

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

At December 31, 2013, our days sales outstanding ("DSOs") were 87 days compared to DSOs of 95 days at December 31, 2012. 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. Accounts receivable at December 31, 2012 included several large billings for retentions associated with appraisal contracts.

Investing activities used cash of \$25.7 million in 2013 compared to \$34.7 million in 2012. Investing activities in 2013 include \$20.3 million paid in connection with the construction of an office building in Plano, Texas compared to \$2.3 million in 2012. In 2012, we completed the acquisitions of Akanda Innovations, Inc., UniFund, L.L.C., Computer Software Associates, Inc. and EnerGov Solutions, L.L.C. The combined cash purchase prices paid in 2012, net of cash acquired was approximately \$25.7 million. In May 2012, we purchased land and a building in Moraine, Ohio to support our appraisal and tax operations for a purchase price of \$2.6 million, which was comprised of \$1.7 million in cash and land and a building valued at \$900,000. These expenditures were funded from cash generated from operations and borrowings under our revolving credit line.

In 2011, we completed the acquisition of Windsor. The purchase price, net of cash acquired, was approximately \$16.4 million. In March 2011, we paid \$6.6 million for approximately 27 acres of land and a building in Plano, Texas.

Financing activities in 2013 provided cash of \$32.0 million compared to cash used by financing activities of \$18.9 million in 2012. Financing activities in 2013 were comprised of \$18.0 million in net payments on our revolving line of credit offset by collections of \$21.8 million from stock option exercises and employee stock purchase plan activity and \$28.2 million excess tax benefit from exercises of share-based arrangements. Cash used in financing activities in 2012 was mainly comprised of \$42.7 million in payments on our revolving line of credit offset by collections of \$15.1 million from stock option exercises and contributions from the employee stock purchase plan and \$8.8 million excess tax benefit from exercises of share-based arrangements.

In 2011, cash used in financing activities was primarily comprised of purchases of treasury shares, net of proceeds from stock option exercises, borrowings and payments on our revolving credit line and contributions from our employee stock purchase plan. During 2011, we purchased 3.0 million shares of our common stock for an aggregate purchase price of \$71.8 million.

The share repurchase program, which was approved by our board of directors, was announced in October 2002, and was amended in April 2003, July 2003, October 2004, October 2005, May 2007, May 2008, October 2008, May 2009, July 2010, October 2010 and September 2011. As of December 31, 2013, we had remaining authorization to repurchase up to 1.7 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, as well as the volume of employee stock option exercises. These share repurchases are funded using our existing cash balances and borrowings under our revolving credit agreement and may occur through open market purchases 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.

In 2013, we issued 1.4 million shares of common stock and received \$18.3 million in aggregate proceeds upon exercise of stock options. In 2012 we issued 1.2 million shares of common stock and received \$12.4 million in aggregate proceeds upon exercise of stock options. In 2011 we received \$3.6 million from the exercise of options to purchase approximately 582,000 shares of our common stock under our employee stock option plan. In 2013, 2012 and 2011 we received \$3.5 million, \$2.6 million and \$2.0 million, respectively, from contributions to the Tyler Technologies, Inc. Employee Stock Purchase Plan.

We have a \$150.0 million Credit Agreement (the "Credit Facility") and a related pledge and security agreement with a group of seven financial institutions, with Bank of America, N.A., as Administrative Agent. The Credit Facility provides for a revolving credit line of \$150.0 million (which may be increased up to \$200.0 million subject to our obtaining commitments for such increase), with a \$25.0 million sublimit for letters of credit. The Credit Facility matures on August 11, 2014. Borrowings under the Credit Facility may be used for general corporate purposes, including working capital requirements, acquisitions and share repurchases.

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

Borrowings under the Credit Facility bear interest at a rate of either (1) the Bank of America's prime rate plus a margin of 1.50% to 2.75% or (2) the 30, 60, 90 or 180-day LIBOR rate plus a margin of 2.50% to 3.75%, with the margin determined by our consolidated leverage ratio. The Credit Facility is secured by substantially all of our assets, excluding real 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, and limits incurrence of additional indebtedness and liens. As of December 31, 2013, we were in compliance with those covenants.

As of December 31, 2013, we had no outstanding borrowings and unused available borrowing capacity of \$148.0 million under the Credit Facility. In addition, as of December 31, 2013, our bank had issued an outstanding letter of credit totaling \$2.0 million. This letter of credit reduces our available borrowing capacity and expires in 2014.

We paid income taxes, net of refunds received, of \$9.3 million in 2013, \$13.1 million in 2012 and \$13.4 million in 2011. We experienced significant stock option exercise activity in 2013 that generated \$28.2 million excess tax benefits. Excess tax benefits reduce tax payments but do not significantly reduce the effective tax rate and can result in limitations on other deductions. The majority of this excess tax benefit was generated in the last half of 2013 and as a result we anticipate a tax refund in 2014 for approximately \$9.7 million. In 2012 and 2011, excess tax benefits were \$8.8 million and \$3.6 million, respectively.

Excluding acquisitions, we anticipate that 2014 capital spending will be between \$12.0 million and \$13.0 million. We expect the majority of this capital spending will consist of computer equipment and software for infrastructure replacements and expansion. We currently do not expect to capitalize significant amounts related to software development in 2014, 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 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 2021. Most leases contain renewal options and some contain purchase options.

Summarized in the table below are our obligations to make future payments under our long-term revolving credit agreement and lease obligations at December 31, 2013 (in thousands):

	2014	2015	2016	2017	2018	Thereafter	Total
Lease obligations	\$5,680	\$4,677	\$4,415	\$3,880	\$1,731	\$2,339	\$22,722

As of December 31, 2013, we do not have any off-balance sheet arrangements, guarantees to third parties or material purchase commitments, except for the operating lease commitments listed.

CAPITALIZATION

At December 31, 2013, our capitalization consisted of no outstanding borrowings and \$246.3 million of shareholders' equity.

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. As of December 31, 2013 we had no outstanding borrowings under the Credit Facility. Borrowings under the Credit Facility bear interest at a rate of either (1) the Bank of America's prime rate plus a margin of 1.50% to 2.75% or (2) the 30, 60, 90 or 180-day LIBOR rate plus a margin of 2.50% to 3.75%, with the margin determined by our consolidated leverage ratio.

CONTROLS AND PROCEDURES

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 Securities and Exchange Commission'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, 2013. 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, 2013.

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, 2013. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control — Integrated Framework (1992 framework)*. Based on our assessment, we concluded that, as of December 31, 2013, Tyler's internal control over financial reporting was effective based on those criteria.

Tyler's internal control over financial reporting as of December 31, 2013 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, 2013, there were no changes in our internal control over financial reporting, as defined in Securities Exchange Act Rule 13a-15(f), that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

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, 2013, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) (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 "Management's 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.

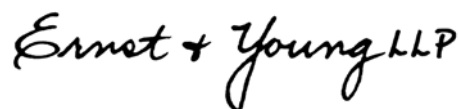
We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material 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, 2013, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Tyler Technologies, Inc. as of December 31, 2013 and 2012, and the related consolidated statements of comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2013 and our report dated February 19, 2014 expressed an unqualified opinion thereon.

The logo for Ernst & Young LLP, featuring the company name in a stylized, handwritten-style script.

Dallas, Texas

February 19, 2014

Report of Independent Registered Public Accounting Firm**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Shareholders

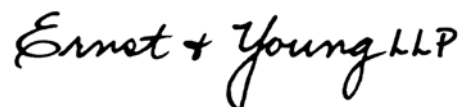
Tyler Technologies, Inc.

We have audited the accompanying consolidated balance sheets of Tyler Technologies, Inc. as of December 31, 2013 and 2012, and the related consolidated statements of comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2013. 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, 2013 and 2012, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2013, 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, 2013, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) and our report dated February 19, 2014 expressed an unqualified opinion thereon.

The signature of Ernst & Young LLP is written in a cursive, handwritten style in black ink.

Dallas, Texas
February 19, 2014

Consolidated Statements of Comprehensive Income

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

For the years ended December 31,	2013	2012	2011
In thousands, except per share amounts			
Revenues:			
Software licenses and royalties	\$ 40,841	\$ 33,928	\$ 32,594
Subscriptions	61,864	44,618	31,160
Software services	93,267	83,408	69,617
Maintenance	191,720	171,851	146,498
Appraisal services	20,825	22,543	23,228
Hardware and other	8,126	6,956	6,294
Total revenues	416,643	363,304	309,391
Cost of revenues:			
Software licenses and royalties	2,377	1,983	3,034
Acquired software	2,078	1,888	1,125
Software services, maintenance and subscriptions	199,617	171,584	143,776
Appraisal services	13,809	14,889	14,550
Hardware and other	5,559	5,258	4,994
Total cost of revenues	223,440	195,602	167,479
Gross profit	193,203	167,702	141,912
Selling, general and administrative expenses	98,289	86,706	75,650
Research and development expense	23,269	20,140	16,414
Amortization of customer and trade name intangibles	4,517	4,279	3,331
Operating income	67,128	56,577	46,517
Other expense, net	1,309	2,709	2,404
Income before income taxes	65,819	53,868	44,113
Income tax provision	26,718	20,874	16,556
Net income	\$ 39,101	\$ 32,994	\$ 27,557
Earnings per common share:			
Basic	\$ 1.23	\$ 1.09	\$ 0.88
Diluted	\$ 1.13	\$ 1.00	\$ 0.83
Unrealized gains (losses) on investment securities available-for-sale	\$ 341	\$ 134	\$ (123)
Income tax expense (benefit) related to components of other comprehensive income (loss)	119	47	(43)
Other comprehensive income (loss), net of tax	\$ 222	\$ 87	\$ (80)
Comprehensive income	\$ 39,323	\$ 33,081	\$ 27,477

See accompanying notes.

Consolidated Balance Sheets

CONSOLIDATED BALANCE SHEETS

December 31,	2013	2012
In thousands, except share and per share amounts		
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 78,876	\$ 6,406
Accounts receivable (less allowance for losses of \$1,113 in 2013 and \$1,621 in 2012)	106,570	99,212
Prepaid expenses	13,522	9,000
Income tax receivable	9,721	406
Other current assets	787	1,074
Deferred income taxes	7,759	5,955
Total current assets	217,235	122,053
Accounts receivable, long-term portion	588	1,187
Property and equipment, net	64,844	45,381
Non-current investments available-for-sale	1,288	2,037
Other assets:		
Goodwill	121,011	121,011
Other intangibles, net	38,986	45,800
Sundry	536	1,197
	\$ 444,488	\$ 338,666
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 2,533	\$ 3,167
Accrued liabilities	32,839	26,018
Deferred revenue	156,738	140,550
Total current liabilities	192,110	169,735
Revolving line of credit	—	18,000
Deferred income taxes	6,059	5,632
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 2013 and 2012	481	481
Additional paid-in capital	182,176	154,018
Accumulated other comprehensive loss, net of tax	(46)	(268)
Retained earnings	202,210	163,109
Treasury stock, at cost; 15,309,940 and 16,816,903 shares in 2013 and 2012, respectively	(138,502)	(172,041)
Total shareholders' equity	246,319	145,299
	\$ 444,488	\$ 338,666

See accompanying notes.

Consolidated Statements of Shareholders' Equity

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

For the years ended December 31, 2013, 2012 and 2011

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock		Total Shareholders' Equity
	Shares	Amount				Shares	Amount	
In thousands								
Balance at December 31, 2010	48,148	\$481	\$153,576	\$(275)	\$102,558	(15,854)	\$(149,368)	\$106,972
Net Income	—	—	—	—	27,557	—	—	27,557
Unrealized loss on investment securities, net of tax	—	—	—	(80)	—	—	—	(80)
Issuance of shares pursuant to stock compensation plan	—	—	(10,352)	—	—	582	13,905	3,553
Stock compensation	—	—	6,253	—	—	—	—	6,253
Treasury stock purchases	—	—	—	—	—	(3,004)	(71,802)	(71,802)
Issuance of shares pursuant to Employee Stock Purchase Plan	—	—	(230)	—	—	100	2,275	2,045
Federal income tax benefit related to exercise of stock options	—	—	3,612	—	—	—	—	3,612
Balance at December 31, 2011	48,148	481	152,859	(355)	130,115	(18,176)	(204,990)	78,110
Net Income	—	—	—	—	32,994	—	—	32,994
Unrealized gain on investment securities, net of tax	—	—	—	87	—	—	—	87
Issuance of shares pursuant to stock compensation plan	—	—	(17,018)	—	—	1,218	29,461	12,443
Stock compensation	—	—	7,411	—	—	—	—	7,411
Issuance of shares pursuant to Employee Stock Purchase Plan	—	—	639	—	—	81	2,002	2,641
Federal income tax benefit related to exercise of stock options	—	—	8,798	—	—	—	—	8,798
Issuance of shares for acquisition	—	—	1,329	—	—	60	1,486	2,815
Balance at December 31, 2012	48,148	481	154,018	(268)	163,109	(16,817)	(172,041)	145,299
Net Income	—	—	—	—	39,101	—	—	39,101
Unrealized gain on investment securities, net of tax	—	—	—	222	—	—	—	222
Issuance of shares pursuant to stock compensation plan	—	—	(13,742)	—	—	1,443	32,031	18,289
Stock compensation	—	—	11,653	—	—	—	—	11,653
Issuance of shares pursuant to Employee Stock Purchase Plan	—	—	2,034	—	—	64	1,508	3,542
Federal income tax benefit related to exercise of stock options	—	—	28,213	—	—	—	—	28,213
Balance at December 31, 2013	48,148	\$481	\$182,176	\$(46)	\$202,210	(15,310)	\$(138,502)	\$246,319

See accompanying notes.

Consolidated Statements of Cash Flows

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended December 31,	2013	2012	2011
In thousands			
Cash flows from operating activities:			
Net income	\$ 39,101	\$ 32,994	\$ 27,557
Adjustments to reconcile net income to net cash provided by operations:			
Depreciation and amortization	13,786	12,711	10,676
Share-based compensation expense	11,653	7,411	6,253
Provision for losses – accounts receivable	729	961	805
Excess tax benefit from exercises of share-based arrangements	(28,207)	(8,764)	(3,590)
Deferred income tax benefit	(1,497)	(215)	(2,916)
Changes in operating assets and liabilities, exclusive of effects of acquired companies:			
Accounts receivable	(7,488)	(6,825)	(8,544)
Income tax receivable	18,898	7,791	6,084
Prepaid expenses and other current assets	(4,154)	110	(214)
Accounts payable	(574)	(369)	575
Accrued liabilities	7,655	(530)	4,887
Deferred revenue	16,188	13,393	14,862
Net cash provided by operating activities	66,090	58,668	56,435
Cash flows from investing activities:			
Proceeds from sale of investments	1,090	75	50
Cost of acquisitions, net of cash acquired	(181)	(25,680)	(17,298)
Additions to property and equipment	(26,858)	(9,102)	(12,278)
Decrease (increase) in other	291	(29)	717
Net cash used by investing activities	(25,658)	(34,736)	(28,809)
Cash flows from financing activities:			
(Decrease) increase in net borrowings on revolving line of credit	(18,000)	(42,700)	34,200
Purchase of treasury shares	—	—	(71,802)
Contributions from employee stock purchase plan	3,542	2,641	2,045
Proceeds from exercise of stock options	18,289	12,443	3,553
Excess tax benefit from exercises of share-based arrangements	28,207	8,764	3,590
Net cash provided (used) by financing activities	32,038	(18,852)	(28,414)
Net increase (decrease) in cash and cash equivalents	72,470	5,080	(788)
Cash and cash equivalents at beginning of period	6,406	1,326	2,114
Cash and cash equivalents at end of period	\$ 78,876	\$ 6,406	\$ 1,326

See accompanying notes.

Notes to Consolidated Financial Statements

(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 software as a service (“SaaS”) arrangements, which utilize the Tyler private cloud, and electronic document filing solutions (“e-filing”). In addition, we also provide property appraisal outsourcing services for taxing jurisdictions.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include our parent company and a subsidiary, which is wholly-owned. All significant intercompany balances and transactions have been eliminated in consolidation.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash on deposit with a bank. Cash and cash equivalents are stated at cost, which approximates market value.

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 accumulated 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 Consolidated Statements of Cash Flows.

REVENUE RECOGNITION

We earn revenue from software licenses, royalties, subscriptions, software services, post-contract customer support (“PCS” or “maintenance”), hardware and appraisal services.

Software Arrangements:

For the majority of our software arrangements, we provide services that range from installation, training, and basic consulting to software modification and customization to meet specific customer needs. 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 relative 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

Notes to Consolidated Financial Statements

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 determine that 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. 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 and Royalties

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, software license 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 and apply the provisions of the Construction — Type and Production — Type Contracts as discussed in ASC 605-35, Multiple Elements Arrangements. 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.

We recognize royalty revenue when earned under the terms of our third party royalty arrangements, provided the fees are considered fixed or determinable and realization of payment is probable. Currently, our third party royalties are variable in nature and such amounts are not considered fixed or determinable until we receive notice of amounts earned. Typically, we receive notice of royalty revenues earned on a quarterly basis in the immediate quarter following the royalty reporting period.

Notes to Consolidated Financial Statements

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 is recognized when we deliver the equipment and collection is probable.

Post-Contract Customer Support

Our customers generally enter into PCS agreements when they purchase our software licenses. PCS includes telephone support, bug fixes, and rights to upgrades on a when-and-if available basis. 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.

Subscription-Based Services:

Subscription-based services consist of revenues derived from SaaS arrangements, which utilize the Tyler private cloud, and electronic filing transactions.

For SaaS arrangements, we evaluate whether the customer has the contractual right to take possession of our software at any time during the hosting period without significant penalty and whether the customer can feasibly maintain the software on the customer's hardware or enter into another arrangement with a third party to host the software. In cases where the customer has the contractual right to take possession of our software at any time during the hosting period without significant penalty and the customer 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.

For SaaS arrangements that do not meet the criteria for recognition under ASC 985-605, we account for the elements under ASC 605-25, Multiple Element Arrangements, using all applicable facts and circumstances, including whether (i) the element has stand-alone value, (ii) there is a general right of return and (iii) the revenue is contingent on delivery of other elements. We allocate contract value to each element of the arrangement that qualifies for treatment as a separate element based on VSOE, and if VSOE is not available, third party evidence, and if third party evidence is unavailable, estimated selling price. We recognize hosting services ratably over the term of the arrangement, which range from one to 10 years but are typically for a period of three to six years. For professional services associated with SaaS arrangements that we determine do not have stand-alone value to the customer or are contingent on delivery of other elements, we recognize the services revenue ratably over the remaining contractual period once we have provided the customer access to the software and we may begin billing for 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.

Electronic filing transaction fees primarily pertain to documents filed with the courts by attorneys and other third parties via our e-filing services and retrieval of filed documents via our access services. The elements for these arrangements are accounted for under ASC 605-25. For each document filed with a court, the filer generally pays a transaction fee and a court filing fee to us and we remit a portion of the transaction fee and the filing fee to the court. We record as revenue the transaction fee, while the portion of the transaction fee remitted to the courts is recorded as cost of sales as we are acting as a principal in the arrangement. Court filing fees collected on behalf of the courts and remitted to the courts are recorded on a net basis and thus do not affect the statement of comprehensive income. In some cases, we are paid on a fixed fee basis and recognize the revenue ratably over the contractual period.

Notes to Consolidated Financial Statements

Costs of performing services under subscription-based arrangements are expensed as incurred, except for certain direct and incremental contract origination and set-up costs associated with SaaS arrangements. Such direct and incremental costs are capitalized and amortized ratably over the related SaaS hosting term.

Appraisal Services:

For our property appraisal projects, we recognize revenue using the proportional 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.

Allocation of Revenue in Statements of Comprehensive Income

In our statements of comprehensive income, 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.

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 our contracts generally provide for the payment for the 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 such as commissions associated with arrangements for which revenue recognition has been deferred. 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

Notes to Consolidated Financial Statements

assumptions include the application of the percentage-of-completion and proportional 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 \$23.3 million during 2013, \$20.1 million during 2012 and \$16.4 million during 2011.

We reduced our research and development expense by approximately \$1.0 million in 2012 and, \$3.5 million in 2011, 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 more likely than not 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 generally vest after three to six 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

Goodwill represents the excess of the purchase price over the fair value of net assets acquired, including identifiable intangible assets, in connection with our business combinations. Upon acquisition, goodwill is assigned to the reporting unit that is expected to benefit from the synergies of the business combination, which is the reporting unit to which the related acquired technology is assigned. A reporting unit is the operating segment, or a business unit one level below that operating segment, for which discrete financial information is prepared and regularly reviewed by executive management. We assess goodwill for impairment annually as of April, or more frequently whenever events or changes in circumstances indicate its carrying value may not be recoverable.

When testing goodwill for impairment quantitatively, we first compare the fair value of each reporting unit with its carrying amount. If the carrying amount of a reporting unit exceeds its fair value, a second step is performed to measure the amount of potential impairment. In the second step, we compare the implied fair value of reporting unit goodwill with the carrying amount of the reporting unit's goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized. The fair values calculated in our impairment

Notes to Consolidated Financial Statements

tests are determined using discounted cash flow models involving several assumptions. 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.

Our annual goodwill impairment analysis, which we performed quantitatively during the second quarter of 2013, 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. 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 of the product for general release to customers. 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. We have not capitalized any internal software development costs in any of the periods presented.

FAIR VALUE OF FINANCIAL INSTRUMENTS

Cash and cash equivalents, accounts receivables, accounts payables, short-term obligations 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, 2013 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 available-for-sale and accounts receivable from trade customers. Our cash and cash equivalents primarily consists of operating account balances, which are maintained at one major financial institution

Notes to Consolidated Financial Statements

and the balances often exceed insured amounts. As of December 31, 2013 we had cash and cash equivalents of \$78.9 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, 2013.

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,	2013	2012	2011
Balance at beginning of year	\$1,621	\$ 990	\$ 1,603
Provisions for losses – accounts receivable	729	961	805
Collection of accounts previously reserved	—	—	(142)
Deductions for accounts charged off or credits issued	(1,237)	(330)	(1,276)
Balance at end of year	\$1,113	\$ 1,621	\$ 990

The termination clauses in most of our contracts provide for the payment for the 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 proportional performance accounting in which the revenue is earned based upon activities performed in one accounting period but the billing normally occurs subsequently 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 \$10.8 million and \$11.8 million at December 31, 2013 and 2012, respectively. We also have recorded retention receivables of \$2.6 million and \$1.3 million at December 31, 2013 and 2012, respectively, 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 included with accounts receivable, long-term portion in the accompanying consolidated 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

Notes to Consolidated Financial Statements

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. 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.

RECLASSIFICATIONS

Certain amounts for previous years have been reclassified to conform to the current year presentation.

(2) ACQUISITIONS

2012

In November 2012, we acquired all of the capital stock of EnerGov Solutions, L.L.C. ("EnerGov") that develops and sells enterprise permitting, land management, licensing and regulatory software solutions to governmental agencies. The purchase price, net of cash acquired of \$15,000 was \$10.5 million in cash and 60,000 shares of Tyler common stock valued at \$2.8 million, based on the stock price on the acquisition date. As of December 31, 2012 the purchase price allocation was not yet complete. In March 2013, we finalized the purchase price allocation, which resulted in additional goodwill of \$1.1 million and a corresponding reduction in tangible assets. The balance sheet at December 31, 2012 has been retrospectively revised to include this adjustment.

In April 2012, we acquired all of the capital stock of Computer Software Associates, Inc. ("CSA") for a cash purchase price of \$9.4 million, net of cash acquired of \$437,000. CSA is a reseller of Tyler's Infinite Visions school enterprise solution, and sells proprietary CSA tax and recording solutions to county governments, primarily in the Northwest.

In March 2012, we acquired all the capital stock of UniFund, L.L.C. ("UniFund") for a cash purchase price of \$4.6 million, net of cash acquired of \$780,000. UniFund provides enterprise resource planning solutions to schools and local governments, primarily in the Northeast. UniFund is also a reseller of Tyler's Infinite Visions school enterprise solution.

In January 2012, we acquired substantially all of the assets of Akanda Innovation, Inc., ("Akanda") a provider of web-based solutions to the public sector, which are integrated, with our property tax software, for a total purchase price of \$2.9 million. The purchase price included certain liabilities we assumed of approximately \$800,000, resulting in net cash paid to the sellers of \$2.1 million, of which \$900,000 was paid prior to December 31, 2011.

2011

In October 2011, we acquired all of the capital stock of Windsor Management Group, L.L.C. for a cash purchase price of \$16.4 million, net of cash acquired of \$7.4 million. Windsor provides Infinite Visions suite of school enterprise solutions for the K-12 education market, primarily in the Southwest.

(3) FAIR VALUE OF FINANCIAL INSTRUMENTS

Assets recorded at fair value in the balance sheet as of December 31, 2013 are categorized based upon the level of judgment associated with the inputs used to measure their fair value as defined by ASC 820, Fair Value Measurements and Disclosures. We have investments available-for-sale (consisting of auction rate securities) that are considered to be Level 3 assets for which little or no market data exist and are required to be measured at fair value on a recurring basis. The fair value of our investments available-for-sale as of December 31, 2013 and December 31, 2012 was \$1.3 million and \$2.0 million, respectively. As of December 31, 2013 the par value of our investments available-for-sale was \$1.4 million and the related temporary impairment was \$72,000, based on our estimate of the related fair value using a discounted trinomial model.

Notes to Consolidated Financial Statements

In association with this estimate of fair value, we have recorded an after-tax temporary unrealized gain on our investments available-for-sale of \$222,000, net of related tax effects of \$119,000 in 2013, which is included in accumulated other comprehensive loss on our balance sheet. The unrealized gain includes the impact of adjusting previously recorded unrealized losses of approximately \$138,000 net of related tax effects of \$74,000 as of December 31, 2013 for one security, which was partially redeemed at par during 2013.

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, 2010	\$2,126
Transfers into level 3	—
Transfers out of level 3	(25)
Purchases, sales issuances and settlements	(25)
Unrealized losses included in accumulated loss	(123)
Balance as of December 31, 2011	1,953
Transfers into level 3	—
Transfers out of level 3	—
Purchases, sales issuances and settlements	(50)
Unrealized gains included in accumulated loss	134
Balance as of December 31, 2012	2,037
Transfers into level 3	—
Transfers out of level 3	—
Purchases, sales issuances and settlements	(1,090)
Unrealized gains included in accumulated loss	341
Balance as of December 31, 2013	\$1,288

(4) PROPERTY AND EQUIPMENT, NET

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

	Useful Lives (Years)	2013	2012
Land	—	\$ 7,800	\$ 7,800
Building and leasehold improvements	5-39	50,523	33,299
Computer equipment and purchased software	3-5	27,071	24,036
Furniture and fixtures	5	10,834	8,108
Transportation equipment	5	241	274
		96,469	73,517
Accumulated depreciation and amortization		(31,625)	(28,136)
Property and equipment, net		\$ 64,844	\$ 45,381

Depreciation expense was \$6.4 million during 2013, \$5.6 million during 2012 and \$5.3 million during 2011.

We own office buildings in Yarmouth, Maine, Lubbock and Plano, Texas, and Moraine, Ohio. We lease some space in these buildings to third-party tenants. These leases expire between 2014 and 2017 and are expected to provide rental income of approximately \$834,000 during 2014, \$685,000 during 2015, \$319,000 during 2016 and \$46,000 during 2017. Rental income associated with third party tenants was \$704,000 in 2013, \$586,000 in 2012 and \$1.2 million in 2011, and was included as a reduction of selling, general and administrative expenses.

Notes to Consolidated Financial Statements

(5) GOODWILL AND OTHER INTANGIBLE ASSETS

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

	2013	2012
Gross carrying amount of acquisition intangibles:		
Customer related intangibles	\$ 60,547	\$ 60,547
Software acquired	32,003	32,003
Trade name	3,109	3,272
Lease acquired	1,387	1,387
	97,046	97,209
Accumulated amortization	(58,060)	(51,489)
Acquisition intangibles, net	\$ 38,986	\$ 45,720
Post acquisition software development costs	\$ 36,701	\$ 36,701
Accumulated amortization	(36,701)	(36,621)
Post acquisition software costs, net	\$ —	\$ 80
Total other intangibles	\$ 38,986	\$ 45,800

Total amortization expense, for acquisition related intangibles and post acquisition software development costs, was \$6.8 million in 2013, \$6.5 million during 2012, and \$4.9 million during 2011.

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

	December 31, 2013			December 31, 2012		
	Gross Carrying Amount	Weighted Average Amortization Period	Accumulated Amortization	Gross Carrying Amount	Weighted Average Amortization Period	Accumulated Amortization
Non-amortizable intangibles:						
Goodwill	\$121,011	—	\$ —	\$121,011	—	\$ —
Amortizable intangibles:						
Customer related intangibles	60,547	15 years	28,864	60,547	15 years	24,554
Software acquired	32,003	5 years	26,584	32,003	5 years	24,505
Trade name	3,109	15 years	1,225	3,272	15 years	1,182
Lease acquired	1,387	5 years	1,387	1,387	5 years	1,248

The changes in the carrying amount of goodwill for the two years ended December 31, 2013 are as follows:

	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Total
Balance as of December 31, 2011	\$100,504	\$ 5,590	\$106,094
Goodwill acquired during 2012 related to the purchase of Akanda	—	967	967
Goodwill acquired during 2012 related to the purchase of UniFund	1,055	—	1,055
Goodwill acquired during 2012 related to the purchase of CSA	4,634	—	4,634
Goodwill acquired during 2012 related to the purchase of EnerGov	8,261	—	8,261
Balance as of December 31, 2012 and December 31, 2013	\$114,454	\$ 6,557	\$121,011

Notes to Consolidated Financial Statements

Estimated annual amortization expense relating to acquisition intangibles, including acquired software for which the amortization expense is recorded as cost of revenues is as follows:

Years ending December 31,	
2014	\$6,308
2015	6,128
2016	6,039
2017	5,042
2018	4,366

(6) ACCRUED LIABILITIES

Accrued liabilities consist of the following at December 31:

	2013	2012
Accrued wages, bonuses and commissions	\$25,471	\$17,875
Other accrued liabilities	7,368	8,143
	<u>\$32,839</u>	<u>\$26,018</u>

(7) REVOLVING LINE OF CREDIT

On August 11, 2010, we entered into a new \$150.0 million Credit Agreement (the "Credit Facility") and a related pledge and security agreement with a group of seven financial institutions, with Bank of America, N.A., as Administrative Agent. The Credit Facility provides for a revolving credit line of \$150.0 million (which may be increased up to \$200.0 million subject to our obtaining commitments for such increase), with a \$25.0 million sublimit for letters of credit. The Credit Facility matures on August 11, 2014. Borrowings under the Credit Facility may be used for general corporate purposes, including working capital requirements, acquisitions and share repurchases.

Borrowings under the Credit Facility bear interest at a rate of either (1) the Bank of America's prime rate plus a margin of 1.50% to 2.75% or (2) the 30, 60, 90 or 180-day LIBOR rate plus a margin of 2.50% to 3.75%, with the margin determined by our consolidated leverage ratio. The Credit Facility is secured by substantially all of our assets, excluding real 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, and limits incurrence of additional indebtedness and liens. As of December 31, 2013, we were in compliance with those covenants.

As of December 31, 2013, we had no outstanding borrowings and unused available borrowing capacity of \$148.0 million under the Credit Facility. In addition, as of December 31, 2013, we had an outstanding letter of credit totaling \$2.0 million. Some of our customers require a letter of credit guaranteeing performance in connection with our contracts. The notional amount of performance guarantees outstanding as of December 31, 2013 was estimated to be approximately \$29.0 million. This letter of credit is issued under our revolving line of credit and reduces our available borrowing capacity. We do not believe this letter of credit will be required to be drawn upon. The letter of credit expires in 2014.

We paid interest of \$899,000 in 2013 and \$2.0 million in 2012.

Notes to Consolidated Financial Statements

(8) INCOME TAX

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

Years ended December 31,	2013	2012	2011
Current:			
Federal	\$25,625	\$19,113	\$17,239
State	2,590	1,976	2,233
	28,215	21,089	19,472
Deferred	(1,497)	(215)	(2,916)
	\$26,718	\$20,874	\$16,556

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

Years ended December 31,	2013	2012	2011
Federal income tax expense at statutory rate	\$23,037	\$18,854	\$15,440
State income tax, net of federal income tax benefit	2,371	1,365	1,238
Non-deductible business expenses	1,110	1,087	918
Qualified manufacturing activities	—	(717)	(840)
Research and development credit	—	—	(177)
Other, net	200	285	(23)
	\$26,718	\$20,874	\$16,556

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

	2013	2012
Deferred income tax assets:		
Operating expenses not currently deductible	\$ 7,360	\$ 5,372
Stock option and other employee benefit plans	7,089	6,097
Capital loss and credit carryforward	185	275
Property and equipment	149	570
Total deferred income tax assets	14,783	12,314
Deferred income tax liabilities:		
Intangible assets	(12,910)	(11,838)
Other	(173)	(153)
Total deferred income tax liabilities	(13,083)	(11,991)
Net deferred income tax asset	\$ 1,700	\$ 323

At December 31, 2013, we had approximately \$650,000 of net operating loss carryforwards for Federal income tax reporting purposes available to offset future taxable income. The \$650,000 was attributable to excess tax benefits related to share-based arrangements for which authoritative guidance prohibits the recognition of a deferred tax asset. The \$650,000 tax benefit will be accounted for as an increase to shareholders' equity and a reduction in income tax payable when realized. This carryforward expires in 2034. We recognized approximately \$28.2 million excess tax benefits related to share-based arrangements in 2013 as a credit to shareholders' equity and a reduction in income taxes payable.

Although realization is not assured, we believe it is more likely than not that all the deferred tax assets at December 31, 2013 and 2012 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.

Notes to Consolidated Financial Statements

The Internal Revenue Service (“IRS”) is examining our U.S. income tax return for the year 2010. We are unable to make a reasonable estimate as to when cash settlements related to the examination, if any, will occur.

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 2009. We are no longer subject to state and local income tax examinations by tax authorities for the years before 2008.

We paid income taxes, net of refunds received, of \$9.3 million in 2013, \$13.1 million in 2012, and \$13.4 million in 2011.

(9) SHAREHOLDERS' EQUITY

The following table details activity in our common stock:

	Years ended December 31,					
	2013		2012		2011	
	Shares	Amount	Shares	Amount	Shares	Amount
Stock option exercises	1,443	\$ 18,289	1,218	\$ 12,443	582	\$ 3,553
Purchases of common stock	—	—	—	—	(3,004)	(71,802)
Employee stock plan purchases	64	3,542	81	2,641	100	2,045
Shares issued for acquisition	—	—	60	2,815	—	—

As of February 19, 2014 we had authorization from our board of directors to repurchase up to 1.7 million additional shares of our common stock.

(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 generally vest after three to six 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, 2013, there were 1.1 million shares available for future grants under the plan from the 16.0 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. The expected life represents the weighted-average period the stock options are expected to be outstanding based primarily on the options' vesting terms, remaining contractual life and the employees' expected exercise based on historical patterns.

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.

Notes to Consolidated Financial Statements

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 share-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,	2013	2012	2011
Expected life (in years)	6.4	6.7	6.7
Expected volatility	32.4%	32.6%	33.1%
Risk-free interest rate	1.4%	1.0%	1.7%
Expected forfeiture rate	3%	3%	3%

The following table summarizes share-based compensation expense related to share-based awards which is recorded in the statements of comprehensive income:

Years ended December 31,	2013	2012	2011
Cost of software services, maintenance and subscriptions	\$ 1,509	\$ 1,084	\$ 871
Selling, general and administrative expense	10,144	6,327	5,382
Total share-based compensation expense	11,653	7,411	6,253
Tax benefit	(3,363)	(2,040)	(1,545)
Net decrease in net income	\$ 8,290	\$ 5,371	\$ 4,708

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, 2010	5,836	\$12.74		
Granted	831	26.83		
Exercised	(582)	6.10		
Forfeited	(26)	15.78		
Outstanding at December 31, 2011	6,059	15.31		
Granted	930	43.53		
Exercised	(1,218)	10.22		
Forfeited	(60)	28.07		
Outstanding at December 31, 2012	5,711	20.86		
Granted	1,453	67.08		
Exercised	(1,443)	12.68		
Forfeited	(1)	68.17		
Outstanding at December 31, 2013	5,720	34.66	7	\$385,868
Exercisable at December 31, 2013	1,971	\$15.41	5	\$170,956

We had unvested options to purchase 3.5 million shares with a weighted average grant date exercise price of \$44.55 as of December 31, 2013 and unvested options to purchase 2.8 million shares with a weighted average grant date exercise price of \$27.20 as of December 31, 2012. As of December 31, 2013, we had \$48.3 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 four years.

Notes to Consolidated Financial Statements

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

	2013	2012	2011
Weighted average grant-date fair value of stock options granted	\$ 23.27	\$ 15.24	\$ 9.91
Total intrinsic value of stock options exercised	99,393	40,589	12,289

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, 2013, there were 1.0 million shares available for future grants under the ESPP from the 2.0 million shares previously approved by the stockholders.

(11) EARNINGS PER SHARE

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

Years Ended December 31,	2013	2012	2011
Numerator for basic and diluted earnings per share:			
Net income	\$39,101	\$32,994	\$27,557
Denominator:			
Weighted-average basic common shares outstanding	31,891	30,327	31,267
Assumed conversion of dilutive securities:			
Stock options	2,699	2,589	1,887
Denominator for diluted earnings per share – Adjusted weighted-average shares	34,590	32,916	33,154
Earnings per common share:			
Basic	\$ 1.23	\$ 1.09	\$ 0.88
Diluted	\$ 1.13	\$ 1.00	\$ 0.83

Stock options representing the right to purchase common stock of 62,000 shares in 2013, 463,000 shares in 2012, and 714,000 shares in 2011 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 an entity owned by an executive's father and brother. The executive does not have an interest in the entity that leases the property to us and the lease arrangement existed at the time we acquired the business unit that occupies this property. Most of our leases are non-cancelable operating lease agreements and they expire at various dates through 2021. In addition to rent, the leases generally require us to pay taxes, maintenance, insurance and certain other operating expenses.

Rent expense was approximately \$7.5 million in 2013, \$7.2 million in 2012, and \$5.9 million in 2011, which included rent expense associated with related party lease agreements of \$1.7 million in 2013, \$1.7 million in 2012, and \$1.8 million in 2011.

Notes to Consolidated Financial Statements

Future minimum lease payments under all non-cancelable leases at December 31, 2013 are as follows:

Years ending December 31,

2014	\$ 5,680
2015	4,677
2016	4,415
2017	3,880
2018	1,731
Thereafter	2,339
	\$ 22,722

Included in future minimum lease payments are non-cancelable payments due to related parties of \$1.7 million in 2014, \$1.7 million in 2015, \$1.7 million in 2016 and \$1.7 million in 2017.

(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 operating results \$3.8 million during 2013, \$3.3 million during 2012, and \$2.9 million during 2011.

(14) COMMITMENTS AND CONTINGENCIES

Other than routine litigation incidental to our business, there are no material legal proceedings pending to which we are party or to which any of our properties are subject.

(15) 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 and state governments.

We provide our software systems and services and appraisal services through four business units which focus on the following products:

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

In accordance with ASC 280-10, Segment Reporting, the financial management and education software solutions unit, financial management and municipal courts and land and vital records software solutions unit and the courts and justice software solutions unit meet the criteria for aggregation and are presented in one reportable segment, Enterprise Software Solutions ("ESS"). The ESS segment provides municipal and county governments and schools with software systems and services 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 ("ATSS") 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.

Notes to Consolidated Financial Statements

We evaluate performance based on several factors, of which the primary financial measure is business segment operating income. We define segment operating income for our business units as income before noncash amortization of intangible assets associated with their acquisition, 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. Corporate segment operating income also includes revenues and expenses related to a company-wide user conference. 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 and net property and equipment. Corporate assets consist of cash and investments, prepaid insurance, intangibles associated with acquisitions, deferred income taxes and net property and equipment mainly related to unallocated information and technology assets.

ESS segment capital expenditures in 2013, 2012 and 2011 included \$19.6 million, \$3.0 million and \$6.6 million, respectively for the construction of a new building and purchase of an existing building and land in connection with plans to consolidate workforces and support long-term growth. ATSS segment capital expenditures in 2012 included \$2.6 million for the purchase of a building and land to support long-term growth.

As of and year ended December 31, 2013	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Corporate	Totals
Revenues				
Software licenses and royalties	\$ 38,774	\$ 2,067	\$ —	\$ 40,841
Subscriptions	59,070	2,794	—	61,864
Software services	85,459	7,808	—	93,267
Maintenance	175,180	16,540	—	191,720
Appraisal services	—	20,825	—	20,825
Hardware and other	6,342	—	1,784	8,126
Intercompany	2,899	—	(2,899)	—
Total revenues	\$367,724	\$50,034	\$ (1,115)	\$416,643
Depreciation and amortization expense	10,569	1,028	2,189	13,786
Segment operating income	85,045	9,428	(20,750)	73,723
Capital expenditures	22,457	250	3,438	26,145
Segment assets	\$161,923	\$16,244	\$266,321	\$444,488
As of and year ended December 31, 2012				
Revenues				
Software licenses and royalties	\$ 32,060	\$ 1,868	\$ —	\$ 33,928
Subscriptions	43,319	1,299	—	44,618
Software services	76,103	7,305	—	83,408
Maintenance	155,290	16,561	—	171,851
Appraisal services	—	22,543	—	22,543
Hardware and other	5,297	—	1,659	6,956
Intercompany	2,249	—	(2,249)	—
Total revenues	\$314,318	\$49,576	\$ (590)	\$363,304
Depreciation and amortization expense	9,929	958	1,824	12,711
Segment operating income	71,135	8,498	(16,889)	62,744
Capital expenditures	5,469	3,382	1,865	10,716
Segment assets	\$134,160	\$18,464	\$186,042	\$338,666

Notes to Consolidated Financial Statements

As of and year ended December 31, 2011	Enterprise Software Solutions	Appraisal and Tax Software Solutions and Services	Corporate	Totals
Revenues				
Software licenses and royalties	\$ 30,194	\$ 2,400	\$ —	\$ 32,594
Subscriptions	30,400	760	—	31,160
Software services	60,840	8,777	—	69,617
Maintenance	130,999	15,499	—	146,498
Appraisal services	—	23,228	—	23,228
Hardware and other	5,199	—	1,095	6,294
Intercompany	2,103	—	(2,103)	—
Total revenues	\$259,735	\$50,664	\$ (1,008)	\$309,391
Depreciation and amortization expense	8,516	650	1,510	10,676
Segment operating income	56,856	9,786	(15,669)	50,973
Capital expenditures	11,143	137	998	12,278
Segment assets	\$119,595	\$20,535	\$155,261	\$295,391

Reconciliation of reportable segment operating income to the Company's consolidated totals:

	2013	2012	2011
Total segment operating income	\$73,723	\$62,744	\$50,973
Amortization of acquired software	(2,078)	(1,888)	(1,125)
Amortization of customer and trade name intangibles	(4,517)	(4,279)	(3,331)
Other expense, net	(1,309)	(2,709)	(2,404)
Income before income taxes	\$65,819	\$53,868	\$44,113

(16) QUARTERLY FINANCIAL INFORMATION (unaudited)

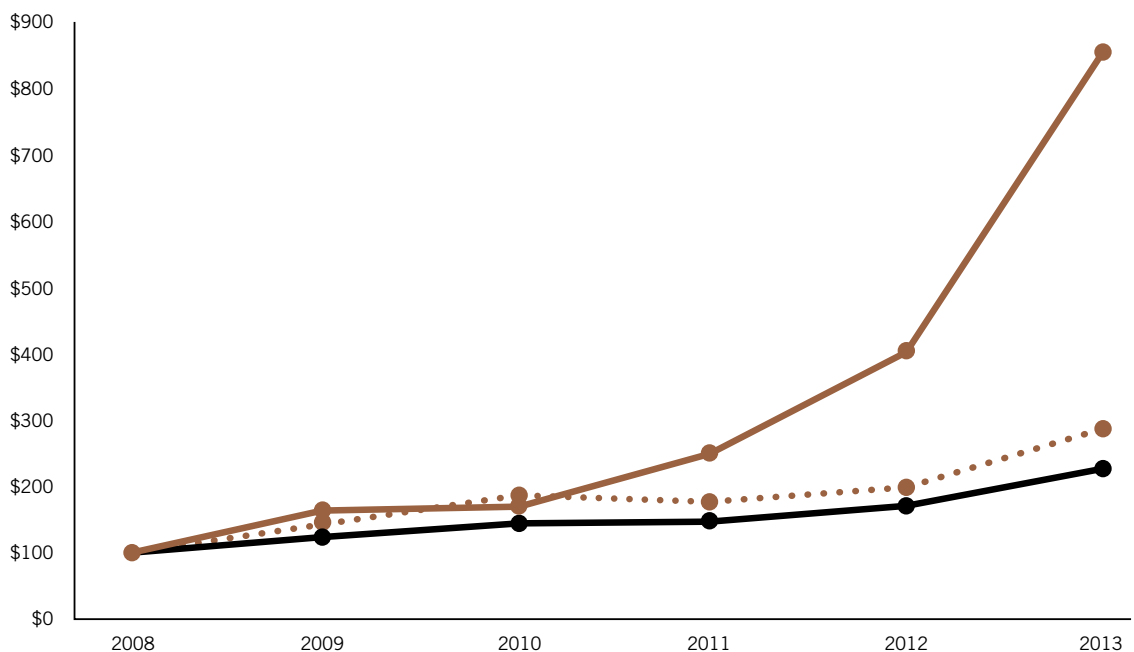
The following table contains selected financial information from unaudited statements of income for each quarter of 2013 and 2012.

Quarters ended	2013				2012			
	Dec. 31	Sept. 30	June 30	Mar. 31	Dec. 31	Sept. 30	June 30	Mar. 31
Revenues	\$110,735	\$107,021	\$103,088	\$95,799	\$95,368	\$93,845	\$91,368	\$82,723
Gross profit	52,767	49,549	47,042	43,845	44,640	44,944	40,699	37,419
Income before income taxes	19,062	17,572	15,053	14,132	15,035	17,810	11,682	9,341
Net income	10,512	11,049	9,047	8,493	9,376	10,832	7,105	5,681
Earnings per diluted share	0.30	0.32	0.26	0.25	0.28	0.33	0.22	0.17
Shares used in computing diluted earnings per share	35,348	34,764	34,290	33,948	33,421	32,986	32,769	32,530

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, 2008. 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



—●—	100	166.19	173.29	251.34	404.34	852.50
—●—	100	126.46	145.51	148.59	172.37	228.19
—●—	100	148.16	184.60	177.17	198.48	287.61

—●—	Tyler Technologies, Inc.
—●—	S&P 500 Index
—●—	S&P 600 Information Technology Index

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

Matthew B. Bieri
Vice President
Chief Information Officer

Samantha B. Crosby
Vice President
Chief Marketing Officer

Robert J. Sansone
Vice President
Human Resources

W. Michael Smith
Vice President
Chief Accounting Officer

Terri L. Alford
Controller

Division Leadership

Andrew D. Teed
President
Appraisal & Tax and
ERP & School Divisions

Bruce Graham
President
Courts & Justice Division

Christopher P. Hepburn
Senior Vice President
ERP & School Division

Brett Cate
President
Local Government Division

Note: Richard E. Peterson Jr., president, ERP & School Division, retired on December 31, 2013.



Board of Directors

John M. Yeaman¹
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}
Chief Operating Officer
Republic Title of Texas, Inc.

Dustin R. Womble¹
Executive Vice President
Tyler Technologies, Inc.

¹ Executive Committee

² Audit Committee

³ Nominating and Governance Committee

⁴ Compensation Committee

Corporate Headquarters

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Plano, Texas 75024
972.713.3700
www.tylertech.com

Transfer Agent and Registrar

American Stock Transfer
& Trust Company
59 Maiden Lane
Plaza Level
New York, New York 10038
800.937.5449
718.236.2641 fax
www.amstock.com

Independent Registered Public

Accounting Firm

Ernst & Young LLP
Dallas, Texas

Annual Meeting of Stockholders

Our annual meeting will be held on
Wednesday, May 14, 2014, at 9:30 a.m.
CDT at The Westin Stonebriar, 1549
Legacy Drive, Frisco, Texas 75034.

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

972.713.3714
info@tylertech.com

Common Stock

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



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Empowering people who serve the public®

