

SONIC FOUNDRY INC
Form 10-K
December 04, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal period ended September 30, 2009

OR

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

Commission File Number 1-14007

SONIC FOUNDRY, INC.

(Exact name of registrant as specified in its charter)

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MARYLAND
(State or other jurisdiction of
incorporation or organization)

39-1783372
(I.R.S. Employer
Identification No.)

222 W. Washington Ave, Madison, WI 53703
(Address of principal executive offices)

(608) 443-1600
(Issuer's telephone number)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common stock par value \$0.01 per share

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

The aggregate market value of the registrant's common stock held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the Registrant's most recently completed second fiscal quarter was approximately \$21,860,000.

The number of shares outstanding of the registrant's common equity was 3,606,922 as of December 1, 2009.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2009 Annual Meeting of Stockholders are incorporated by reference into Part III. A definitive Proxy Statement pursuant to Regulation 14A will be filed with the Commission no later than January 28, 2010.

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<u>Explanatory Note:</u>	

Effective November 16, 2009, Sonic Foundry, Inc. implemented a one-for-ten reverse split of its stock. All share amounts and per share data in this Annual Report on Form 10-K have been adjusted to reflect this reverse stock split.

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When used in this Report, the words anticipate , expect , plan , believe , seek , estimate and similar expressions are intended to identify forward-looking statements. These are statements that relate to future periods and include, but are not limited to, statements about the features, benefits and performance of our Rich Media products, our ability to introduce new product offerings and increase revenue from existing products, expected expenses including those related to selling and marketing, product development and general and administrative, our beliefs regarding the health and growth of the market for Rich Media products, anticipated increase in our customer base, expansion of our products functionalities, expected revenue levels and sources of revenue, expected impact, if any, of legal proceedings, the adequacy of liquidity and capital resources, and expected growth in business. Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those projected. These risks and uncertainties include, but are not limited to, market acceptance for our products, our ability to attract and retain customers and distribution partners for existing and new products, our ability to control our expenses, our ability to recruit and retain employees, the ability of distribution partners to successfully sell our products, legislation and government regulation, shifts in technology, global and local business conditions, our ability to effectively maintain and update our products and service portfolio, the strength of competitive offerings, the prices being charged by those competitors, and the risks discussed elsewhere herein. These forward-looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

PART I

ITEM 1. BUSINESS

Who We Are

Sonic Foundry, Inc. is a web communications technology leader, providing webcasting, lecture capture and knowledge management solutions for higher education institutions, businesses and government agencies worldwide. Powered by our patented webcasting platform, Mediasite®, Sonic Foundry empowers people to transform the way they communicate. We help our customers connect within a dynamic, evolving world of shared knowledge and envision a future where learners and workers around the globe use webcasting to bridge time and distance; accelerate research, productivity and growth; and reduce the environmental impact of traditional education and business communications.

Sonic Foundry solutions include:

Mediasite Recorders for capturing multimedia presentations

Mediasite EX Server platform for streaming, archiving and managing online presentation content

Sonic Foundry Event Services for turnkey event webcasting based on the Mediasite platform

Sonic Foundry Services for hosting, installation, training and custom development

Mediasite Customer Assurance for annual hardware and software maintenance and technical support

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Today, nearly 1,800 customers using more than 3,500 Mediasite Recorders in presentation venues around the world are capturing hundreds of thousands of multimedia presentations with millions of viewers.

Sonic Foundry, Inc. was founded in 1991, incorporated in Wisconsin in March 1994 and merged into a Maryland corporation of the same name in October 1996. Our executive offices are located at 222 West Washington Ave., Madison, Wisconsin 53703 and our telephone number is (608) 443-1600. Our corporate website is www.sonicfoundry.com. In the Investor Information section of our website we make available, free of charge, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to reports required to be filed pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as soon as reasonably practicable after the filing of such reports with the Securities and Exchange Commission.

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Challenges We Address

Every organization faces a fundamental need to communicate information efficiently to individuals who need it. Universities and colleges need to connect lecturers with students for advanced learning. Corporations strive for successful communication and collaboration between colleagues to provide value to customers. Government agencies must keep partners, stakeholders and constituents informed to operate effectively. And yet, communication and e-learning challenges remain, including:

Ensuring students' academic and professional success

Enabling learners to watch or review course material to improve retention and positively impact grades

Providing distance learners with the same quality education as on-campus students

Helping students balance education, career and family commitments

Increasing enrollment without the expense of new classrooms and facilities

Capturing complex graphics where visual clarity is essential for learning
Connecting with a geographically-dispersed audience

Simultaneously addressing people in multiple locations

Holding meetings when it is not feasible for everyone to attend

Transmitting timely information that is crucial for all to receive

Requiring employees, regardless of time zone or schedule, to attend training
Improving productivity and overall organizational knowledge

Avoiding the need for participants to leave their desks to attend a meeting or training

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Maintaining productivity while in training

Reducing time to train new hires

Increasing retention by avoiding distractions, interruptions or absence

Keeping everyone on the same page to prevent false starts and forgotten directives

Documenting meeting content for later review

Maintaining a rich library of organizational knowledge

Documenting and preserving expertise from a retiring workforce
Reducing logistical and financial impacts

Cutting travel expenses and carbon footprints

Eliminating repetition of the same presentation to different audiences

Reducing repeated costs for printing, mailing and meeting expenses
Avoiding cumbersome and restrictive technologies

Maintaining the way presenters present without requiring technical expertise in presentation systems

Capturing and sharing knowledge in real-time without pre-authoring or pre-uploading of content or needing substantial post-production time

Removing significant time and specialized expertise to manage presentation systems

Sonic Foundry Solutions

Sonic Foundry is changing the way organizations share and use information. Our solutions include:

Mediasite Recorders for capturing multimedia presentations

Mediasite EX Server platform for streaming, archiving and managing online presentation content

Sonic Foundry Event Services for turnkey event webcasting based on the Mediasite platform

Sonic Foundry Services for hosting, installation, training and custom development

Mediasite Customer Assurance for annual hardware and software maintenance and technical support

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Mediasite Recorders are designed with presenters in mind. They automatically record what presenters say and show, without changing how they present, and webcast it online. Mediasite Recorders automate the capture and delivery of any presenter's audio, video and presentation graphics as high resolution, interactive presentations that can be immediately watched via the web—live or on-demand. The result is the industry's simplest workflow, eliminating time-consuming authoring, slide uploads and post-production work. Plus, seamless integration with existing audio/video and educational technology means organizations can confidently scale multimedia webcasting throughout their academic or corporate enterprise.

We offer Mediasite Recorders for the following environments:

A room-based Mediasite Recorder (RL Series) for presentation facilities like conference and training rooms, lecture halls, auditoriums and classrooms

A mobile Mediasite Recorder (ML Series) for portability to off-site events, conferences, trade shows or multiple venues throughout an organization

Accompanying all Mediasite Recorders is the Mediasite Editor, a desktop software tool allowing users to edit their presentations, if desired, before publishing them to the web.

Mediasite EX Server Platform is a powerful platform for delivering and managing live and on-demand webcasts. It greatly simplifies content management by providing a single system to schedule, catalog, customize, secure, track and integrate recorded presentations. It brings order and control to valuable content libraries by making it easy to manage hundreds of system users, thousands of recorded hours and as many viewers as needed.

Mediasite EX Server allows organizations to:

Save time and staffing by scheduling presentations to be automatically recorded without an operator

Automatically create customizable and searchable online content catalogs without web development or integration skills

Secure presentations and Mediasite system access for authorized users

Customize and brand their presentation content, incorporate audience interactivity through polls and Q&A

Support closed captions to provide viewers a richer presentation experience while meeting federal or state accessibility mandates

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Track and report on viewing activity to see who is watching what presentations when and to analyze viewing patterns that may correlate to improved learning outcomes, increased performance or program effectiveness

Centrally monitor and control the recording functions of multiple simultaneous Mediasite Recorders for increased operator efficiency

Integrate Mediasite content into other course/learning/contentmanagement systems, web portals, blogs or online community sites

Leverage existing network technologies for content distribution efficiency and performance

Reliably scale to meet the webcasting needs of departmental and enterprise-wide implementations alike

Choose the deployment model that best suits their environment, whether on-premise or hosted in the Sonic Foundry datacenter
Sonic Foundry Event Services equips customers with a team of trained technicians who work on-site to webcast conferences and events. Event webcasting:

Enhances attendee experience with online presentation catalogs

Reaches a wider audience, making presentations available to those not able to attend

Brands presentations using organization logos, colors and messages

Reviews a real-time record of what took place

Links handout materials with the full presentation, including audio, video and graphics

Offers sample content to entice new attendees to participate

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Sonic Foundry Services enable organizations to quickly and easily take advantage of the Mediasite platform, without having to wade through the IT or network complexities associated with their own infrastructure. Sonic Foundry Services include:

Hosting or Software as a Service (SaaS): Our pay-as-you-go service offerings provide content hosting, delivery and management of Mediasite content using Sonic Foundry's data center and infrastructure. These managed services allow organizations of all sizes to jump start their web communications initiatives quickly and simply. They provide a low-risk way to implement online multimedia communications before bringing hosting requirements in-house and can offer a hassle-free long-term solution.

Installation: Sonic Foundry provides onsite consulting and installation services to help customers optimize their deployment and efficiently integrate Mediasite within their existing AV and IT infrastructures, processes and workflows.

Training: To maximize customers' return on investments, skilled trainers provide the necessary knowledge transfer so organizations feel confident in using, managing and leveraging Mediasite's capabilities. On-site training is customized to specific requirements and skill levels, while online training provides convenient anytime access to a web-based catalog of training modules.

Custom Development: Sonic Foundry streamlines how Mediasite interfaces with a customer's specific technologies, internal policies, workflow or content delivery systems through project-based development.

Mediasite Customer Assurance provides customers annually renewable maintenance and support plans for their Mediasite solutions giving them access to Sonic Foundry technical expertise and Mediasite software updates. With a Mediasite Customer Assurance contract, customers are entitled to:

Software upgrades and updates for Mediasite Recorders and Servers

Unlimited technical support assistance

Extension of their recorder hardware warranty

Advanced Recorder hardware replacement

Authorized access to the Mediasite Customer Assurance Portal where they can access software available for download, documentation, knowledge base articles, tutorials, online training and technical resources at any time.

The majority of our customers purchase a Customer Assurance plan when they purchase Mediasite Recorders or Servers.

What Sets Mediasite Apart?

Ease of use We believe that presenters should not need to know anything about the technology that is facilitating their online communication. Automated or schedule-based recording simplifies what has previously been a technical and complex workflow. As a result, presenters can present as they normally do, which enables non-technical, line of business and subject matter experts to feel comfortable communicating via Mediasite. Similarly, viewers need nothing more than a web browser to watch Mediasite presentations.

Comprehensive content management We understand the need to bring order to a growing presentation library so content can be found, used and re-purposed to derive maximum value. Organizations must find ways to manage that content, and Sonic Foundry believes a complete solution focuses not only on the recording of knowledge, but also the retention and management of that knowledge in a system specifically designed for rich media. Mediasite automatically creates searchable online catalogs that index and organize presentations with customizable playback experiences. With integration support for leading enterprise directories, all content can be secured to allow/deny access to specific groups or individuals based on roles and permissions. Mediasite also allows organizations to track and generate reports for every presentation and/or user of the system, letting them see exactly who is watching what, when and how long.

Reliability Whether starting at the department level with a couple rooms or at the enterprise level with a campus- or company-wide implementation, Mediasite was developed to be the single platform to confidently and reliably scale to organizations' webcasting needs. Nearly 1,800 customers around the world depend on Mediasite and its proven design to webcast critical information, enrich daily communications and retain their organizational knowledge.

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Dynamic multimedia experience The Mediasite experience takes into account different individual learning styles – auditory, visual and kinesthetic – providing an interactive format that engages the viewer via different modalities to increase content comprehension and retention. We understand that learning materials and supporting visuals come in many different forms, and Mediasite Recorders’ flexible capture options support input from any laptop application, tablet PC, electronic whiteboard, document camera, medical instrumentation and more. (Many other webcast solutions focus on PowerPoint as the predominant or only source of content and may not support video.) In November 2006, the United States Patent and Trademark Office granted Sonic Foundry a patent on Mediasite’s unique method to capture and automatically index and synchronize what the presenter says (audio and video) with visual aids (RGB-based presentation content) and instantly stream them both over the Internet. Mediasite is also the first lecture capture solution to offer a fully Microsoft® Silverlight®-enabled Player which provides a more dynamic, user-controlled viewing experience. Adding to Mediasite’s interactivity is the ability to incorporate polls, Q&A or links to other related reference materials supporting the learning process. Support for video closed captioning benefits those with hearing disabilities, but also allows all users to use keyword search to pinpoint and play back content of interest within a Mediasite presentation.

Software as a Service (SaaS) deployment option To minimize IT challenges, network infrastructure issues and expertise required to install, configure and maintain Mediasite within the enterprise, Sonic Foundry hosting provides organizations a low-risk method of using the complete Mediasite platform within a state-of-the-art datacenter.

Customer service Sonic Foundry and the growing Mediasite community provide a reliable, collaborative support network for all Mediasite customers. Our breadth of field-based system engineers and responsive customer care ensure that customers have readily available resources committed to their success. The Mediasite User Group (MUG), now over 900 members strong, is one of the most vibrant, diverse and rapidly expanding user communities for lecture capture, online training and e-learning. MUG members share ideas and get feedback from community experts through online forum discussions, participate in live quarterly meetings to exchange best practices and network at UNLEASH, the annual Mediasite User Conference.

Sonic Foundry Solutions in Higher Education and the Enterprise

Sonic Foundry solutions are rapidly emerging as the standard for recording, delivering and managing one-to-many multimedia webcasts for higher education and corporate, healthcare or government enterprises

Sonic Foundry solutions in higher education:

Among post-secondary institutions, Mediasite is used for:

Online lectures (blended/hybrid learning): students review content outside of in-class instruction

Distance learning: off-campus students learn remotely online

Continuing education: professionals learn online or supplement classroom experiences

Faculty training and development

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Research and collaboration: faculty document and present findings

Recruitment and orientation: campus tours, financial aid instructions

Special events: commencement, guest speakers

University business: leadership meetings, alumni relations, outreach
Through interviews, many higher education institutions report that Mediasite:

Improves student learning outcomes

Lets students watch and re-watch presentations at their convenience, boosting information retention

Replicates the in-class experience for online students or those unable to attend class

Contributes to enhanced grades

Caters to different learning modalities audio, visual, kinesthetic

Enables their institution to remain competitive

Allows quick development and delivery cost-effective online programs

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Supports higher enrollment and/or tuition without new classrooms

Improves student retention and matriculation

Helps attract students and faculty

Empowers faculty

Allows them to teach as usual without learning new technology

Promotes greater in-class interactivity rather than copious note-taking

Improves student outcomes

Enables knowledge sharing and collaboration with colleagues

Boosts campus outreach

Bolsters recruitment efforts

Captures and preserves campus events

Enhances alumni relations

Given the technology pedigree of today's college students, this move to online learning makes perfect sense as most of these students have never known a world without personal computers and the web. The delivery options for a modern education are akin to the electronic delivery of music that emerged several years ago. Students demand immediate access to their coursework regardless of time or place.

Recent trends such as the slowing economy and lingering high fuel prices continue to drive more students, particularly adult learners, to online education through enrollment in blended or hybrid courses with a traditional on-campus component or through fully online distance learning programs. Historically, graduate programs and STEM (science, technology, engineering and math)-oriented degree programs in schools of medicine, nursing, engineering or business have comprised the majority of the company's academic customer base. We are now experiencing heightened market demand for lecture capture within undergraduate and community college programs as well.

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According to The November 2008 Sloan Consortium report, *Staying the Course: Online Education in the United States, 2008*, online enrollments the past several years have been growing considerably. The 12.9 percent growth rate for online enrollments far exceeds the 1.2 percent growth of the overall higher education student population. In the 2007 fall term, over 3.9 million, or more than 20 percent of all U.S. higher education students, were taking at least one online course, a 12 percent increase over the previous year.

Community colleges, specifically, have significantly increased their number of blended or hybrid and web-enhanced courses. The Instructional Technology Council's 2008 Distance Education Survey Results: *Tracking the Impact of eLearning at Community Colleges* (April 2009) shows that overall, 74 percent of community colleges offer at least one online degree, meaning at least 70 percent of the required course work is offered online. Sixty-four percent of community colleges plan to increase the number of blended courses, for which 30 to 79 percent of course content is delivered online, with some face-to-face meetings. The most recent data indicates no signs of these online learning trends slowing.

In September 2008, Sonic Foundry sponsored a research project with the University of Wisconsin E-Business Institute which resulted in the study, *Insights Regarding Undergraduate Preference for Lecture Capture*. A survey was sent to 29,078 undergraduate and graduate students at the University of Wisconsin-Madison in April 2008. Average response rate exceeded 25 percent. Of the survey participants, a significant number of undergraduates (47 percent) have taken a class in which lectures were recorded and made available online. Eighty-two percent of the undergraduates in the sample strongly preferred a course that records and streams lecture content online versus a course that only features in-room instruction. Students reported better retention, improved ability to review for exams and greater engagement during classes with lecture capture. Over half of the undergraduates indicated that, even after course completion, having course material available online would be important and that there was interest in accessing online material in their professional lives. Over 60 percent of the sample was willing to pay for lecture capture services. Of those willing to pay, the majority of undergraduates (69 percent) expressed a preference to pay on a course-by-course basis rather than having lecture capture fees bundled with existing technology fees.

Several universities have conducted their own independent studies to assess the impact of Mediasite on student performance. Penn State Hershey Medical Center and College of Medicine, a Mediasite campus since January 2004, deployed a pilot program at the

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onset of the 2007-2008 academic year to record lectures to first year medical students. During this academic year, lectures were viewed a total of 22,451 times, averaging 59.1 views per lecture by a class of 154 students. Mediasite use increased throughout the academic year, with 97 percent of students using Mediasite to review lectures by the semester's end. Almost half of the students surveyed (41 percent) cited reviewing complicated material as the number one motivator for using Mediasite. The majority (88 percent) agreed that Mediasite helps them achieve their educational goals. Much fewer (25 percent) said podcasting had the same effect. Faculty members reported that recording their lectures did not decrease class attendance. The survey also revealed a correlation between the grading method and the use of Mediasite. Students watch lectures more often via Mediasite for classes where grades are awarded as honors, high pass, pass and fail versus simply pass/fail.

The Paul Merage School of Business at the University of California, Irvine, surveyed students in its 2007-2008 MBA for Executives and MBA for Health Care Executives programs. Ninety-one percent used Mediasite to view lectures, 71 percent found they were more engaged in lectures when they didn't have to focus on taking copious notes and 83 percent said they learned more in courses when lectures were available on demand. The survey also determined that 93 percent of the students would choose an MBA program that produces mediasite course content over a school with traditional in-class instruction alone. Furthermore, 82 percent would pay higher tuition for a program that streams and archives instruction, with almost half willing to pay between \$2,000 and \$5,000 more for their two-year degree.

To remain relevant, colleges and universities are striving to differentiate themselves through technical leadership as a means to attract these tech-savvy students, while balancing their campus technology improvements with systems that faculty will embrace and adopt. As a result, the education market is beginning to restructure and increase investments around online learning. We believe the visible integration of multimedia learning content into core university applications and the success of bundled online learning technology solutions are two healthy indicators for the widespread adoption of online campus lectures.

To date, Sonic Foundry has installed Mediasite in the larger lecture halls and classrooms of campuses nationwide. We now see more and broader expansions and integrations of Mediasite at the campus-wide level. Course and learning management systems like Blackboard®, Moodle, Desire2Learn®, Angel, or Sakai are ubiquitous in the education enterprise. As the foundation for e-learning, these systems are rapidly moving beyond simply aggregating related course documents (handouts, assignments, course syllabi) to becoming students' single-source portal for all course-related materials including recorded multimedia content like online lectures. Mediasite's packaged integrations for Blackboard and Moodle, the leading course management systems used in higher education, address the need to make learning content accessible to students when and where they need it.

Sonic Foundry Solutions in the Enterprise:

Within medium to large corporate, healthcare and government enterprises, Mediasite has numerous applications.

In corporate enterprises it is used for:

Executive communications: state of the enterprise speeches, all-hands meetings

Workforce development: training, HR briefings, policy documentation

Sales and marketing: demonstrations, product announcements, webinars, channel relations

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Internal knowledge repositories: technical training, research collaboration, user-generated content

Customer support: product tutorials, self-guided troubleshooting

Investor relations: earnings calls, analyst briefings, annual reports

Conferences and events

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In health-related enterprises it is used for:

Education: CME, grand rounds, seminars, student/patient simulations

On-demand medical information

Caregiver training

Emergency response coordination

Public health announcements

Research and collaboration

Conferences and events

In government agencies it is used for:

Program management: relief work, military coordination, emergency preparedness

Community outreach: committee meetings, public safety announcements

Training, workshops and events

Executive and legislative communications: constituent relations, public speeches, debates

Through interviews across these verticals, enterprise customers report that Mediasite:

Expands training and communications opportunities

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Enables them to offer training to more and larger audiences

Captures knowledge from a retiring workforce

Supports the creation and sharing of user-generated content

Aides in building a knowledge library

Extends the life of conferences and events

Cuts travel and meeting expenses

Eliminates redundant speaking engagements

Opens communication channels with dispersed audiences regardless of location or time zone

Provides the ability to address everyone at once

Boosts efficiency

Enables immediate communication of time-sensitive information

Delivers the message directly to the desktop to reduce downtime

Allows participants to watch when it's convenient to avoid interruptions and increase retention

Reduces new hire training time

Helps build stronger teams

Fosters direct management/employee communications

Supports more frequent, clearer communication with colleagues and staff

Keeps all employees aligned

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Cultivates team morale and collaboration

Less than a decade ago, the only people in the enterprise talking openly about online multimedia were AV specialists in IT or media services units, and even these people were skeptical about what benefits streaming would hold for the enterprise. Now, knowledge workers, executives, event planners and people in training, sales, human resources and research and development are pushing for online multimedia and webcasting as part of their e-learning initiatives. They have a business need to be seen and heard by their colleagues, and the return on investment (ROI) for multimedia online learning is real and measurable.

Claire Schooley, senior analyst with Forrester Research, Inc., wrote in the April 2009 report, *The ROI of eLearning*, "Online learning earns companies a positive ROI in less than a year. If you have a business that is spread across many locations, it makes good business sense to implement an online learning program as a replacement for some face-to-face learning and as a complement to other instructor-led training in the form of blended learning. Whether employees take compliance training, desktop skills development, or leadership training, online learning is flexible, consistent, and repeatable with minimal travel costs. The keys to success include excellent eLearning content that engages the learner; good change management plans for this new way of learning; and technology that is scalable and easy to use to manage the learning." She goes on to state that "Outside of subject areas where face-to-face

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interaction is necessary, recent research indicates that no significant differences exist in the effectiveness of learning through classroom, online, or self-study. Self-paced eLearning allows learners to assimilate content at their own speed – often 20% to 50% faster than in a classroom

Gartner vice president and distinguished analyst, Carol Rozwell, echoes the value of e-learning in the January 2009 report, *Key Issues for Corporate Learning Systems, 2009*. She states, “Getting people up to speed quickly and efficiently is critical for all roles, but especially for those positions with a high turnover rate, such as sales and customer support. Reducing time to competency demands that employees, customers and business partners are connected to high-quality learning content so they can achieve workplace performance objectives. In times of financial stress, interest in e-learning increases. It gives learners the opportunity for training without the expense of travel and it allows the company to support green initiatives.

The technology market for enterprise streaming solutions that support many e-learning and business communications initiatives is growing as well. In Wainhouse Research’s, *Enterprise Streaming Products Market Size and Forecast (July 2009)*, senior analyst and partner, Ira Weinstein, estimates the enterprise streaming products market (which includes content capture and management solutions and related services for installation, training and support) to be \$365 million. This market will expand to \$1.039 billion by 2013 with Weinstein projecting annual growth rates to stabilize in the mid-30% range in the latter portion of the 2009-2013 forecast period.

Future Directions

Because webcasting and lecture capture are becoming an everyday part of the way people work and learn, we are driven to shorten the time it takes people not only to capture and share their information but also to find the information they need. While today leading universities use Mediasite for lecture capture and corporations webcast training and executive communications, we envision a future where people around the globe use webcasting to bridge time and distance; accelerate research, productivity and growth; and reduce the environmental impact of traditional education and business communications. As a company, we are helping create the libraries of tomorrow with technology that does not compound the world’s information overload. We are working to put a human face on all online knowledge, and we believe the world will be more knowledgeable and more connected as a result.

Supporting this vision, our ongoing innovations center on:

Developing deployment options to meet the webcasting needs for organizations of all sizes. This includes:

Significant investment, development and evolution of our current Mediasite hosting platform to provide Software as a Service (SaaS). This alternative to traditional on-premise deployments provides an ideal way to minimize IT challenges and potential webcasting risks while affordably extending high performance, fault tolerant webcasting to small and large customers alike.

Content capture innovations that economically scale across entire organizations, allowing anyone to record and share their knowledge or expertise.

Integrating with and embedding Mediasite content into enterprise portals, learning and course management systems, content management repositories, blogs and online communities.

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Enabling context-based viewing of multimedia webcasts within online environments that enable and encourage discussion around the content and synchronized with it.

Supporting content playback experiences on additional platforms and popular mobile computing devices.

Evolving Mediasite's content management capabilities to accommodate organizations' existing digital video assets.

Continuing development of keyword search within and across archived multimedia presentations.

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Segment Information

We have determined that in accordance with FASB ASC-280-10, we operate in only one segment as we do not disaggregate profit and loss information on a segment basis for internal management reporting purposes to our chief operating decision maker. Therefore, such information is not presented.

We have included the cash effect of billings not recorded as revenue, which are deferred for GAAP purposes, in arriving at non-GAAP net income or loss. Our services are typically billed and collected in advance of providing the service which requires minimal cost to perform in the future. Billings are a better indicator of customer activity and cash flow than revenue is, in management's opinion, and is therefore used by management as a key operational indicator. Billings is computed by combining revenue with the change in unearned revenue. Total billings for Mediasite product and support outside the United States totaled 28 percent and 19 percent in 2009 and 2008, respectively.

Our largest individual customers are typically value added resellers (VARs) and distributors since the majority of our end users require additional complimentary products and services which we do not provide. Accordingly, in fiscal 2009 and 2008 a master distributor, Synnex Corporation (Synnex), contributed 29 percent and 44 percent, respectively, of total world-wide billings. As a master distributor, Synnex fulfills transactions to VARs, end users and other distributors. No other customer represented over 10 percent in 2008 or 2009.

Sales

We sell and market our offerings through a sales force that manages a channel of value-added resellers, system integrators, consultants and distributors. These third party representatives specialize in understanding both audio/video systems and IT networking. In fiscal 2009, we utilized two master distributors in the U.S. and over 100 resellers, and sold our products to nearly 1,000 total end users. Our focus has been primarily in the United States and primarily to customers we have identified as having the greatest potential for high use; that is, organizations with presenters, trainers, lecturers, marketers and leaders who have a routine need to communicate to many people in higher education, government, health and certain corporate markets. Despite our primary attention on the North American market, reseller and customer interest outside of North America has grown and accordingly, we allocated three sales professionals to address international demand. To date, we have sold our products to customers in over 40 countries outside the United States. Total billings for Mediasite product and support outside the United States totaled 28 percent and 19 percent in fiscal 2009 and 2008, respectively.

Vertical market expansion: Over half our revenue is realized from the education market. Recent trends such as high gas prices and the slowing economy are driving more students, particularly adult learners, to seek online education options. Similarly, demand for lecture capture within undergraduate, community college and blended learning programs is beginning to demonstrate growth. This development represents an emerging trend beyond the traditional academic customer base for the company, which has primarily consisted of graduate, distance learning and technical degree programs.

For our higher education as well as corporate, government and association clients, we anticipate weakening economic conditions will expand market demand for more outsourced services versus licensed sales. Over the last two years, the company has made extensive capital and technology investments to advance its services model with turnkey event webcasting, comprehensive hosting/Software as a Service (SaaS), and e-commerce capabilities that position us well to deliver more diversified business services.

With the launch of our Event Services group in 2007, we continue to see growing demand for conference and event webcasting. These event-based communication, education and training applications, combined with outsourced webcasting services, are expected to drive the company's corporate sales activities going forward.

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Repeat orders: Many customers initially purchase a small number of Mediasite Recorders to test or pilot in a department, school or business unit. A successful pilot project and the associated increase in webcasting demand from other departments or schools leads to follow up, multiple Recorder orders as well as increased Mediasite Server capacity. In fiscal 2009, 62 percent of billings were to preexisting customers compared to 59 percent in fiscal 2008.

Renewals: As is typical in the industry, we offer annual support and maintenance service contract extensions for a fee to our customer base.

Marketing

Marketing efforts span the spectrum of product demonstrations, tradeshow, websites, webinars, brochures, direct mail, e-mail campaigns, newsletters, print and online advertising, sponsorships, white papers and analyst relations. We often request and receive press release quotes and written or multimedia testimonials from satisfied, high-profile reference customers, particularly those that demonstrate innovative and valuable uses of the Mediasite platform and Event Services. We solicit respected industry magazines and trade organizations to review our product and use advisors as introductions to new channels or customers. We have a large, growing database of potential customers in the education, government and corporate marketplaces and have established a process of targeting specific verticals that have a direct and demonstrated need for our offerings.

Operations

We contract with third parties to build the hardware of our Mediasite Recorders and purchase quantities sufficient to fill specific customer orders, including purchases of inventory by resellers. Quantities are maintained in inventory by the third party providers and shipped directly to the end customer or reseller. The hardware manufacturers provide a limited one-year warranty on the hardware, which we pass on to our customers who purchase a Mediasite Customer Assurance support and maintenance plan. We have an alternate source of manufacturing for some of the products we produce and believe there are numerous additional sources and alternatives to the existing production process. To date, we have not experienced any material difficulties or delays in the manufacture and assembly of our products or material returns due to product defects.

OTHER INFORMATION

Competition

In the lecture capture and webcasting market we face competition from various companies that provide related, but different, communication technologies. These include:

Web conferencing includes solutions from Adobe, Cisco (WebEx), Microsoft and Citrix. Although part of the overall online multimedia communications landscape, these solutions are designed primarily for collaborative communications versus one-to-many communications like Mediasite. Many organizations acknowledge that they need both technologies – one-to-many webcasting and collaborative web conferencing – to appropriately address their different communication requirements.

Video conferencing includes solutions from Polycom, TANDBERG (now Cisco) and Sony. These solutions are designed primarily for one-to-one or group communications with high levels of interactivity and collaboration. Like web conferencing, many organizations use both video conferencing and webcasting. Mediasite integrates with videoconferencing endpoints from Polycom and TANDBERG to record and manage interactive meetings, discussions and distance learning courses alongside other Mediasite content.

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Authoring tools include solutions like Accordent PresenterPLUS, Camtasia Studio and Microsoft Producer. Unlike webcasting, web conferencing or video conferencing, which are forms of online multimedia communication that capture and distribute/stream content, these solutions are production-oriented tools designed to create and edit multimedia content only. Some organizations will

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use these desktop tools to create training content by manually integrating existing audio, video, images, branding and other visual elements into a multimedia presentation which can then be published to a web or streaming server for distribution. This process can require a significant amount of production effort and user expertise in presentation authoring.

Online video services and virtual meeting platforms include solutions from inXpo, Livestream, ON24, Stream57, Thomson Reuters, Unisfair and Wall Street Webcasting. These companies offer services or SaaS-based platforms that either allow audio and video to be captured from a presenter's computer (often with supporting materials uploaded in advance), produced streaming video services or 2D/3D virtual environments that may or may not include rich media webcasts.

Other vendors such as Echo360, Tegrity, Accordent Technologies and Panopto, provide lecture capture or webcasting capabilities, but differ in their technology approach, particularly in the lecture capture arena. Mediasite is an appliance- or room-based platform for lecture capture. It provides a full integrated system designed around an automated purpose-built recording appliance that captures, publishes and manages rich media content. Room-based appliances are capable of streaming live or on-demand and can leverage the full breadth of in-room audio/visual technology. Transparent recording automation means no presenter intervention which leads to the broadest end-user adoption across campus. A room-based platform like Mediasite also includes a complete content management platform for captured multimedia presentations. Other lecture capture solutions are implemented as software applications designed to capture and publish rich media content, but dependent upon a third-party content management platform, typically the institution's course management system. Software applications for lecture capture support on-demand streaming only and require in-room PC integration with varying levels of presenter intervention and recording knowledge which may lead to lower adoption rates throughout the campus. Lastly, laptop-resident desktop tools capture and publish non-rich media (limited video and presentation graphics). Like software applications they support on-demand streaming only and require a third-party content management platform. Desktop tools require the greatest degree of presenter intervention, technical confidence and support. While prevalent on many campuses, these three factors limit the practicality for campus-wide adoption.

Some current and potential customers have developed their own home-grown webcasting or lecture capture solutions which may compete with Mediasite. However, we often find many of these organizations are now looking for a solution that requires less internal maintenance and effort, offers comprehensive management capabilities and a less cumbersome workflow.

The more successful we are in the growing market for lecture capture and webcasting, the more competitors are likely to emerge. We believe that the principal competitive factors in our market include:

Ease of use and application transparency to the user

Content management and scalability to address enterprise requirements

Reliability and performance

Security of content, applications and services

Ability to integrate with third-party solutions and services

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Flexible deployment and acquisition options to suit various budgets

Customer service and support

A significant reference-able customer base

Ability to introduce new products and services to the market in a timely manner

Two leading industry analyst firms recognize Sonic Foundry's Mediasite as the leading, best-of-breed platform for lecture capture. Frost & Sullivan awarded Sonic Foundry consecutive Market Leadership Awards for Lecture Capture based on the market analyses in their World Presentation Assembly and Management Platforms reports (2009 and 2007). The Frost & Sullivan Award for Market Leadership is given to the company that exhibits market share leadership through the implementation of market strategy. Wainhouse Research also recognizes Mediasite as a streaming and lecture capture market leader for distance education and elearning in their report, The Distance Education and e-Learning Landscape V2 (December 2008). Among Wainhouse's evaluation criteria are innovation, market understanding, overall viability, product strategy and customer experience. According to the report, Sonic Foundry ranks highest from the perspective of depth of overall blend of products and ranks among the leaders in its ability to execute.

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Intellectual Property

The status of United States patent protection in the Internet industry is not well defined and will evolve as the U.S. Patent and Trademark Office grants additional patents. Currently two U.S. patents that have been issued to us, and four U.S. patent applications are pending. We may seek additional patents in the future. We do not know if our pending patent applications or any future patent application will result in any patents being issued with the scope of the claims we seek, if such patents are issued at all. We do not know whether the patents which were recently approved or any patents we may receive in the future will be challenged, invalidated or be of any value. It is difficult to monitor unauthorized use of technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States, and our competitors may independently develop technology similar to ours. We will continue to seek patent and other intellectual property protections, when appropriate, for those aspects of our technology that we believe constitute innovations providing significant competitive advantages. Our pending, and any future, patent applications may not result in the issuance of valid patents.

Our success depends in part upon our rights to proprietary technology. We rely on a combination of copyright, trade secret, trademark and contractual protection to establish and protect our proprietary rights. We have registered seven U.S. and four foreign country trademarks. We require our employees to enter into confidentiality and nondisclosure agreements upon commencement of employment. Before we will disclose any confidential aspects of our services, technology or business plans to customers, potential business distribution partners and other non-employees, we routinely require such persons to enter into confidentiality and nondisclosure agreements. In addition, we require all employees, and those consultants involved in the deployment of our services, to agree to assign to us any proprietary information, inventions or other intellectual property they generate, or come to possess, while employed by us. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain and use our services or technology. These precautions may not prevent misappropriation or infringement of our intellectual property.

Third parties may infringe or misappropriate our copyrights, trademarks and similar proprietary rights. In addition, we may be subject to claims of alleged infringement of patents and other intellectual property rights of third parties. We may be unaware of filed patent applications which have not yet been made public and which relate to our services.

Intellectual property claims may be asserted against us in the future. Intellectual property litigation is expensive and time-consuming and could divert management's attention away from running our business. Intellectual property litigation could also require us to develop non-infringing technology or enter into royalty or license agreements. These royalty or license agreements, if required, may not be available on acceptable terms, if at all. Our failure or inability to develop non-infringing technology or license the proprietary rights on a timely basis would harm our business.

Research and Development

We believe that our future success will depend in part on our ability to continue to develop new business, and to enhance our existing business. Accordingly, we invest a significant amount of our resources in research and development activities. During each of the fiscal years ended September 30, 2009 and 2008, we spent \$3.5 million on internal research and development activities in our business. These amounts represent 19% and 23%, respectively, of total revenue in each of those years.

Employees

As of September 30, 2009 and 2008, we had 93 and 91 full-time employees, respectively. Our employees are not represented by a labor union, nor are they subject to a collective bargaining agreement. We have never experienced a work stoppage and believe that our employee relations are satisfactory.

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ITEM 1A. RISK FACTORS

YOU SHOULD CAREFULLY CONSIDER THE RISKS DESCRIBED BELOW BEFORE MAKING AN INVESTMENT DECISION. THE RISKS DESCRIBED BELOW ARE NOT THE ONLY ONES WE FACE. ADDITIONAL RISKS THAT WE ARE NOT PRESENTLY AWARE OF OR THAT WE CURRENTLY BELIEVE ARE IMMATERIAL MAY ALSO IMPAIR OUR BUSINESS OPERATIONS. OUR BUSINESS COULD BE HARMED BY ANY OR ALL OF THESE RISKS. THE TRADING PRICE OF OUR COMMON STOCK COULD DECLINE SIGNIFICANTLY DUE TO ANY OF THESE RISKS, AND YOU MAY LOSE ALL OR PART OF YOUR INVESTMENT. IN ASSESSING THESE RISKS, YOU SHOULD ALSO REFER TO THE OTHER INFORMATION CONTAINED OR INCORPORATED BY REFERENCE IN THIS ANNUAL REPORT ON FORM 10-K, INCLUDING OUR CONSOLIDATED FINANCIAL STATEMENTS AND RELATED NOTES.

Economic conditions could materially adversely affect the Company.

The Company's operations and performance depend significantly on worldwide economic conditions. Uncertainty about current global economic conditions poses a risk as businesses, educational institutions and government entities may cancel or postpone spending in response to tighter credit, negative financial news, declines in income or asset values and/or reduced public sector funding, which could have a material negative effect on the demand for the Company's products and services and on the Company's financial condition and operating results.

The current financial turmoil affecting the banking system and financial markets have resulted in a tightening in the credit markets, a low level of liquidity in many financial markets, and extreme volatility in fixed income, credit, currency and equity markets. There could be a number of follow-on effects from the credit crisis on the Company's business, including insolvency of key suppliers resulting in products delays, inability of customers, including channel partners, to obtain credit to finance purchases of the Company's products and/or customer, including channel partner insolvencies; and inability of our channel partners and other customers to pay accounts receivable owed to us, or delays in the payment of such receivables. Additionally, if these economic conditions persist, our intangible assets may be impaired. If we determine that the fair value of intangible assets is less than its carrying value, we would then measure impairment based on a comparison of the implied fair value of the intangible assets with the carrying amount of the intangible assets. To the extent the carrying amount is greater than the implied fair value, we would record an impairment charge for the difference.

Economic conditions may have a disproportionate affect on the sale of our products.

Many of our customers will look at the total A/V equipment and labor cost to outfit a typical conference room or lecture hall as one amount for budgetary purposes. Consequently, although our products represent only a portion of the total cost, the entire project of outfitting a room or conference hall may be considered excessive and may not survive budgetary constraints. Alternatively, our resellers may modify their quotes to end customers by eliminating our products or substituting less expensive competitive products in order to win opportunities within budget constraints. Event service partners may similarly suggest that customers eliminate recording and webcasting as a means of reducing event cost. Consequently, declines in spending by government, educational or corporate institutions due to budgetary constraints may have a disproportionate impact on the Company and result in a material adverse impact on our financial condition.

We may need to raise additional capital if we do not quickly become profitable.

At September 30, 2009 we had cash of \$2.6 million and availability under our line of credit facility with Silicon Valley Bank of \$0.8 million. The Company has historically financed its operations primarily through cash from sales of equity securities, cash from operations, and to a limited extent, through bank credit facilities. The Company has incurred losses from operations in each of the last three fiscal years. In response to the recurring operating losses, the Company initiated cost reduction efforts in January 2008. These efforts achieved a reduction in quarterly operating expenses of approximately 24%. The Company anticipates operating expenses to

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remain at or near these reduced levels in fiscal 2010. The Company achieved billings growth in fiscal 2009 of approximately 8% over 2008 and believes its cash position is adequate to accomplish its business plan through at least the next twelve months even if billings are unchanged from fiscal 2009.

We may evaluate further operating or capital lease opportunities to finance equipment purchases in the future and expect to utilize the Company's revolving line of credit to support working capital needs. While the Company anticipates that it will be in compliance with all provisions of the agreement, there can be no assurance that the existing Loan Agreement will remain available to the Company nor that additional financing will be available or on terms acceptable to the Company.

The business environment is not currently conducive to raising additional debt or equity financing and may not improve in the near term. If we borrow money, we may incur significant interest charges, which could harm our profitability. Holders of debt would also have rights, preferences or privileges senior to those of existing holders of our common stock. If we raise additional equity, the terms of such financing may dilute the ownership interests of current investors and cause our stock price to fall significantly. We may not be able to secure financing upon acceptable terms, if at all. If we cannot raise funds on acceptable terms, we may not be able to develop or enhance our products, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements, which could seriously harm our business, operating results, and financial condition.

We have a history of losses.

For the year ended September 30, 2009, we had a gross margin of \$14.2 million on revenue of \$18.6 million with which to cover selling, marketing, product development and general administrative costs. Our selling, marketing, product development and general administration costs have historically been a significant percentage of our revenue, due partly to the expense of developing leads and the relatively long period required to convert leads into sales associated with selling products that are not yet considered mainstream technology investments. For the years ended September 30, 2009 and 2008 our cash used in operations was (\$1.5) and (\$3.9) million, respectively. Although we expect our operations to continue to improve in fiscal 2010, we may never achieve or sustain profitability on a quarterly or annual basis.

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

Most of our customers and potential customers are public colleges, universities, schools and other education providers who depend substantially on government funding. Accordingly, any general decrease, delay or change in federal, state or local funding for colleges, universities, schools and other education providers could cause our current and potential customers to reduce their purchases of our products and services, or to decide not to renew service contracts, either of which could cause us to lose revenues. In addition, a specific reduction in governmental funding support for products such as ours would also cause us to lose revenues. The severe economic downturn experienced in the U.S. and globally has caused many of our clients to experience severe budgetary pressures, which has and will likely continue to have a negative impact on sales of our products. Continuing unfavorable economic conditions may result in further budget cuts and lead to lower overall spending, including information technology spending, by our current and potential clients, which may cause our revenues to decrease. In addition, our accounts receivable may increase and the relative aging of our receivables may deteriorate if our clients delay or are unable to make their payments due to the tightening of credit markets and the lack of available funding. Also, because many of our clients begin their fiscal year in July or later, easing of budgetary pressure may not occur until late fiscal 2010.

If we are unable to comply with NASDAQ's continued listing requirements, our common stock could be delisted from the NASDAQ Capital Market.

In March 2008, our common stock failed to maintain a minimum bid price of \$1.00 for at least 10 consecutive days, which caused our stock price to fail to meet one of the minimum standards required by the NASDAQ Stock Market for continued listing as a NASDAQ Global Market security. On March 10, 2008 we received a letter from NASDAQ indicating that we need to regain compliance with the minimum bid price requirement by September 8, 2008 in order to remain on the NASDAQ Global Market. On September 9, 2008

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we were notified by NASDAQ that we had failed to regain compliance with the minimum bid price during the 180 days provided and our securities were therefore subject to delisting from the NASDAQ Global Market. In response, we applied for and were notified on September 12, 2008 by NASDAQ that NASDAQ approved our request to transfer the listing of our shares to the NASDAQ Capital Market. Transfer to the NASDAQ Capital Market and compliance with its initial listing standards afforded an additional 180 day period for our stock to attain the minimum \$1.00 bid price for at least 10 consecutive business days until March 9, 2009. We received notice from NASDAQ on October 22, 2008, December 23, 2008 and March 24, 2009 that NASDAQ had determined to extend the suspension of the minimum bid price for additional 90 day periods. On July 14, 2009, we received notice from NASDAQ that enforcement of the minimum bid price requirement would be reinstated on August 3, 2009. The Company had 141 calendar days remaining in its bid price compliance period when suspension began, extending the period in which to regain compliance to December 21, 2009. On November 2, 2009 the Company notified NASDAQ that it intended to execute a reverse split of its stock in the ratio of one for ten, effective November 16, 2009. On December 2, 2009, the Company received notice from NASDAQ that the Company had regained compliance with the minimum bid requirement and the matter was now closed. While there is no pending listing compliance issue with NASDAQ, there is no assurance that the Company will not fail one or more listing requirements in the future. If our stock is delisted, it may have a material adverse effect on the price of our common stock and the levels of liquidity currently available to our stockholders. Delisting would also make it more difficult for us to raise capital in the future or impact customer confidence. If our common stock is removed from the NASDAQ Capital Market, an investor could find it more difficult to dispose of, or to obtain accurate quotations as to the market value of, our common shares. Additionally, our stock may then be subject to penny stock regulations.

If a sufficient number of customers do not accept our products, our business may not succeed.

We cannot predict how the market for our products will develop, and part of our strategic challenge will be to convince enterprise customers of the productivity, improved communications, cost savings, suitability and other benefits of our products. Our future revenue and revenue growth rates will depend in large part on our success in delivering these products effectively, creating market acceptance for these products, and meeting customer's needs for new or enhanced products. If we fail to do so, our products will not achieve widespread market acceptance, and we may not generate significant revenue to offset our product development and selling and marketing costs, which will hurt our business.

We may not be able to innovate to meet the needs of our target market.

Our future success will continue to depend upon our ability to develop new products or product enhancements that address future needs of our target markets and to respond to these changing standards and practices. Our revenue could be reduced if we do not capitalize on our current market leadership by timely developing innovative new products or product enhancements that will increase the likelihood that our products will be accepted in preference to the products of our current and future competitors.

Multiple unit sales may fail to materialize.

We need to sell multiple units to educational, corporate and government institutions in order to sell most efficiently and become profitable. In fiscal 2009, 62% of revenue was to existing customers compared to 59% in fiscal 2008. In particular, selling multiple units to corporate customers has lagged results achieved in the higher education market; consequently, we have allocated more resources to the higher education market. While we have addressed a strategy to leverage existing customers and close multiple unit transactions, a customer may choose not to make expected purchases of our products. The failure of our customers to make expected purchases will harm our business.

If our marketing and lead generation efforts are not successful, our business will be harmed.

We believe that continued marketing efforts will be critical to achieve widespread acceptance of our products. Our marketing campaign may not be successful given the expense required. For example, failure to adequately generate and develop sales leads could cause our future revenue growth to decrease. In addition, our inability to generate and cultivate sales leads into large organizations, where there is the potential for significant use of our products, could have a material effect on our business. We may not be able to identify and secure the number of strategic sales leads necessary to help generate marketplace acceptance of our products. If our marketing or lead-generation efforts are not successful, our

business and operating results will be harmed.

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The length of our sales and deployment cycle is uncertain, which may cause our revenue and operating results to vary significantly from quarter to quarter and year to year.

During our sales cycle, we spend considerable time and expense providing information to prospective customers about the use and benefits of our products without generating corresponding revenue. Our expense levels are relatively fixed in the short-term and based in part on our expectations of future revenue. Therefore, any delay in our sales cycle could cause significant variations in our operating results, particularly because a relatively small number of customer orders represent a large portion of our revenue.

Our largest potential sources of revenue are educational institutions, large corporations and government entities that often require long testing and approval processes before making a decision to purchase our products, particularly when evaluating our products for inclusion in new buildings under construction or high dollar transactions. In general, the process of selling our products to a potential customer may involve lengthy negotiations, collaborations with consultants, designers and architects, time consuming installation processes and changes in network infrastructure in excess of what we or our VARs are able to provide. As a result, our sales cycle is unpredictable. Our sales cycle is also subject to delays as a result of customer-specific factors over which we have little or no control, including budgetary constraints and internal approval procedures.

Our products are aimed toward a broadened user base within our key markets and these products are relatively early in their product life cycles. We cannot predict how the market for our products will develop and part of our strategic challenge will be to convince targeted users of the productivity, improved communications, cost savings and other benefits. Accordingly, it is likely that delays in our sales cycles with these products will occur and this could cause significant variations in our operating results.

Sales of some of our products have experienced seasonal fluctuations which have affected sequential growth rates for these products, particularly in our first fiscal quarter. For example, there is generally a slowdown for sales of our products in the higher education and corporate markets in the first fiscal quarter of each year. Seasonal fluctuations could negatively affect our business, which could cause our operating results to fall short of anticipated results for such quarters.

Our operating results are hard to predict as a significant amount of our sales typically occur at the end of a quarter and the mix of product and service orders may vary significantly.

Revenue for any particular quarter is extremely difficult to predict with any degree of certainty. We typically ship products within a short time after we receive an order and therefore, we typically do not have an order backlog with which to estimate future revenue. In addition, orders from our channel partners are based on the level of demand from end-user customers. Any decline or uncertainty in end-user demand could negatively impact end-user orders, which could in turn significantly negatively affect orders from our channel partners in any given quarter. Accordingly, our expectations for both short and long-term future revenue is based almost exclusively on our own estimate of future demand based on the pipeline of sales opportunities we manage, rather than on firm channel partner orders. Our expense levels are based largely on these estimates. In addition, the majority of our orders are received in the last month of a quarter; thus, the unpredictability of the receipt of these orders could negatively impact our future results. We historically have received all or nearly all our channel partner orders in the last month of a quarter and often in the last few days of the quarter. Accordingly, any significant shortfall in demand for our products in relation to our expectations would have an adverse impact on our operating results.

We have experienced growing demand for our hosting and event services as well as a growing preference from our corporate customers in purchasing our solution as a service (SaaS). As a result, we expect that service billings as a percentage of total billings will continue to grow which we believe will ultimately lead to higher gross margins and more recurring revenue. The percentage of billings represented by service is also likely to fluctuate from quarter to quarter due to seasonality of event services and other factors.

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Since services are typically billed in advance of providing the service, revenue is initially deferred, leading to reduced current period revenue with a corresponding negative impact to profits or losses in periods of significant growth in billings for deferred services. An increase, or significant fluctuation, in service billings as a percentage of total billings may therefore lead to a temporary decline in our reported revenue.

We are subject to risks associated with our channel partners product inventories and product sell-through.

We sell a significant amount of our products to Synnex, Starin and other channel partners who maintain their own inventory of our products for sale to dealers and end-users. If these channel partners are unable to sell an adequate amount of their inventory of our products in a given quarter to dealers and end-users or if channel partners decide to decrease their inventories for any reason, such as a recurrence of global economic uncertainty and downturn in technology spending, the volume of our sales to these channel partners and our revenue would be negatively affected. In addition, if channel partners decide to purchase more inventory, due to product availability or other reasons, than is required to satisfy end-user demand or if end-user demand does not keep pace with the additional inventory purchases, channel inventory could grow in any particular quarter, which could adversely affect product revenue in the subsequent quarter. In addition, we also face the risk that some of our channel partners have inventory levels in excess of future anticipated sales. If such sales do not occur in the time frame anticipated by these channel partners for any reason, these channel partners may substantially decrease the amount of product they order from us in subsequent periods, which would harm our business.

If stock balancing returns or price adjustments exceed our reserves, our operating results could be adversely affected.

We provide some of our distributors with stock balancing return rights, which generally permit our distributors to return products, subject to ordering an equal dollar amount of alternate products. We also provide price protection rights to most of our distributors. Price protection rights require that we grant retroactive price adjustments for inventories of our products held by distributors if we lower our prices for those products within a specified time period. To cover our exposure to these product returns and price adjustments, we establish reserves based on our evaluation of historical product trends and current marketing plans. However, we cannot be assured that our reserves will be sufficient to cover our future product returns and price adjustments. If we inadequately forecast reserves, our operating results could be adversely affected.

We depend in part on the success of our relationships with third-party resellers and integrators.

Our success depends on various third-party relationships, particularly with our international and events services operations. The relationships include third party resellers as well as system integrators that assist with implementations of our products and sourcing of our products and services. Identifying partners, negotiating and documenting relationships with them and maintaining their relationships require significant time and resources from us. In addition, our agreements with our resellers and integrators are typically non-exclusive and do not prohibit them from working with our competitors or from offering competing products or services. Our competitors may be effective in providing incentives to third parties to favor their products or services. If we are unsuccessful in establishing or maintaining our relationships with these third parties, our ability to compete in the marketplace or to maintain or grow our revenue could be impaired and our operating results would suffer.

Manufacturing disruption or capacity constraints would harm our business.

We subcontract the manufacture of our recorders to one third-party contract manufacturer and subcontract the manufacture of our rack-unit recorder and a proprietary component with another third-party contract manufacturer. Although we believe there are multiple sources of supply from other contract manufacturers as well as multiple suppliers of component parts required by the contract manufacturers, a short term disruption of supply of component parts or completed products near the end of a quarter would have a negative impact on our revenues. Moreover, any incapacitation of the manufacturing site due to destruction, natural disaster or similar events could result in a loss of product inventory. As a result of any of the foregoing, we may not be able to meet demand for our products, which could negatively affect revenues in the quarter of the disruption or longer depending upon the magnitude of the event, and could harm our reputation.

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Our cash flow could fluctuate due to the potential difficulty of collecting our receivables.

A significant portion of our sales are fulfilled by VARs, regional distributors or master distributors. As an example, 29% of our billings in 2009 were to Synnex, a master distributor who fulfills demand from other distributors, VARs or end users. While our distributors and VARs typically maintain payment terms consistent with other end users, a delay in payment may occur as a result of a number of factors including changes in demand, general economic factors, financial performance, inventory levels or disputes over payments. Any delay from Synnex, or other large distributors or VARs could have a material impact on the collections of our receivables during a particular quarter.

Over the past year we have begun to expand the level of sales representation in Europe and Asia as well as other international regions. We offer credit terms to some of our international customers; however, payments tend to go beyond terms in certain countries. Therefore, as Europe, Asia and other international regions grow as a percentage of our revenue, accounts receivable balances will likely increase as compared to previous years.

Accounting regulations and related interpretations and policies, particularly those related to revenue recognition, cause us to defer revenue recognition into future periods for portions of our products and services.

Revenue recognition for our products and services is complex and subject to multiple sources of authoritative guidance as well as varied interpretations and implementation practices for such rules. These rules require us to defer revenue recognition in certain situations. Factors that are considered in revenue recognition include those such as vendor specific objective evidence (VSOE), the inclusion of other services and contingencies to payment terms. We expect that we will continue to defer portions of our product and service billings because of these factors. The amounts deferred may be significant and will vary each quarter depending on the mix of products sold in each market and geography, as well as the actual contract terms.

Additional changes in authoritative guidance or changes in practice in applying such rules could also cause us to defer the recognition of revenue to future periods or recognize lower revenue

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

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

Because we generally recognize revenues ratably over the term of our service contracts, downturns or upturns in service transactions will not be fully reflected in our operating results until future periods.

We recognize most of our revenues from service contracts monthly over the terms of their agreements, which are typically 12 months, although terms can range from less than one month to over 36 months. As a result, much of the service revenue we report in each quarter is attributable to agreements entered into during previous quarters. Consequently, a decline in sales, client renewals, or market acceptance of our products in any one quarter will not necessarily be fully reflected in the revenues in that quarter, and will negatively affect our revenues and profitability in future quarters. This ratable revenue recognition also makes it difficult for us to rapidly increase our revenues through additional sales in any period, as revenues from new clients must be recognized over the applicable agreement term.

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There is a great deal of competition in the market for our products, which could lower the demand for our products.

In the lecture capture and webcasting market we face competition from various companies that provide related, but different, communication technologies. These include:

Web conferencing includes solutions from Adobe, Cisco (WebEx), Microsoft and Citrix. Although part of the overall online multimedia communications landscape, these solutions are designed primarily for collaborative communications versus one-to-many communications like Mediasite. Many organizations acknowledge that they need both technologies – one-to-many webcasting and collaborative web conferencing – to appropriately address their different communication requirements.

Video conferencing includes solutions from Polycom, TANDBERG (now, Cisco) and Sony. These solutions are designed primarily for one-to-one or group communications with high levels of interactivity and collaboration. Like web conferencing, many organizations use both video conferencing and webcasting. Mediasite integrates with videoconferencing endpoints from Polycom and TANDBERG to record and manage interactive meetings, discussions and distance learning courses alongside other Mediasite content.

Authoring tools include solutions like Accordent PresenterPLUS, Camtasia Studio and Microsoft Producer. Unlike webcasting, web conferencing or video conferencing, which are forms of online multimedia communication that capture and distribute/stream content, these solutions are production-oriented tools designed to create and edit multimedia content only. Some organizations will use these desktop tools to create training content by manually integrating existing audio, video, images, branding and other visual elements into a multimedia presentation which can then be published to a web or streaming server for distribution. This process can require a significant amount of production effort and user expertise in presentation authoring.

Online video services and virtual meeting platforms include solutions from inXpo, Livestream, ON24, Stream57, Thomson Reuters, Unisfair and Wall Street Webcasting. These companies offer services or SaaS-based platforms that either allow audio and video to be captured from a presenter's computer (often with supporting materials uploaded in advance), produced streaming video services or 2D/3D virtual environments that may or may not include rich media webcasts.

Other vendors such as Echo360, Tegrity, Accordent Technologies and Panopto, provide lecture capture or webcasting capabilities, but differ in their technology approach, particularly in the lecture capture arena. Mediasite is an appliance- or room-based platform for lecture capture. It provides a full integrated system designed around an automated purpose-built recording appliance that captures, publishes and manages rich media content. Room-based appliances are capable of streaming live or on-demand and can leverage the full breadth of in-room audio/visual technology. Transparent recording automation means no presenter intervention which leads to the broadest end-user adoption across campus. A room-based platform like Mediasite also includes a complete content management platform for captured multimedia presentations. Other lecture capture solutions are implemented as software applications designed to capture and publish rich media content, but dependent upon a third-party content management platform, typically the institution's course management system. Software applications for lecture capture support on-demand streaming only and require in-room PC integration with varying levels of presenter intervention and recording knowledge which may lead to lower adoption rates throughout the campus. Lastly, laptop-resident desktop tools capture and publish non-rich media (limited video and presentation graphics). Like software applications they support on-demand streaming only and require a third-party content management platform. Desktop tools require the greatest degree of presenter intervention, technical confidence and support. While prevalent on many campuses, these three factors limit the practicality for campus-wide adoption.

The presence of these competitors could reduce the demand for our systems, and we may not have the financial resources to compete successfully.

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

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

Our customers may use our products to share confidential and sensitive information, and if our system security is breached, our reputation could be harmed and we may lose customers.

Our customers may use our products and services to share confidential and sensitive information, the security of which is critical to their business. Third parties may attempt to breach our security for customer hosted content or the networks of our customers. Customers may take inadequate security precautions with their sensitive information and may inadvertently make that information public. We may be liable to our customers for any breach in security, and any breach could harm our reputation and cause us to lose customers. In addition, customers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We may be required to expend significant capital and other resources to further protect against security breaches or to resolve problems caused by any breach, including litigation-related expenses if we are sued.

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

Unanticipated problems affecting our network systems could cause interruptions or delays in the delivery of the hosting services we provide to some of our clients. We provide remote hosting through computer hardware, some of which is within our facility and some of which is currently located in a third-party co-location facility. We do not control the operation of this co-location facility. Lengthy interruptions in our hosting service could be caused by the occurrence of a natural disaster, power loss, vandalism or other telecommunications problems at the co-location facility or if this co-location facility were to close without adequate notice. We currently do not have adequate computer hardware and systems to provide alternative service for most of our hosted clients in the event of an extended loss of service at the co-location facility. We are not equipped to provide full disaster recovery to all of our hosted clients. If there are operational failures in our network infrastructure that cause interruptions, slower response times, loss of data or extended loss of service for our remotely hosted clients, we may be required to issue credits or pay penalties, current clients may terminate their contracts or elect not to renew them, and we may lose sales to potential clients. If we determine that we need additional hardware and systems, we may be required to make further investments in our network infrastructure.

The technology underlying our products and services is complex and may contain unknown defects that could harm our reputation, result in product liability or decrease market acceptance of our products.

The technology underlying our products is complex and includes software that is internally developed, software licensed from third parties and hardware purchased from third parties. These products may contain errors or defects, particularly when first introduced or when new versions or enhancements are released. We may not discover defects that affect our current or new applications or enhancements until after they are sold and our insurance coverage may not be sufficient to cover our complete liability exposure. Any defects in our products and services could:

Damage our reputation;

Cause our customers to initiate product liability suits against us;

Increase our product development resources;

Cause us to lose sales; and

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Delay market acceptance of our products.

If we are viewed only as a commodity supplier, our margins and valuations will shrink.

We need to provide value-added services in order to avoid being viewed as a commodity supplier. This entails building long-term customer relationships and developing features that will distinguish our products. Our technology is complex and is often confused with other products and technologies in the market place, including video conferencing, streaming and collaboration. If we fail to build long-term customer relationships and develop features that distinguish our products in the market place, our margins will shrink, and our stock may become less valued to investors.

Our success depends upon the proprietary aspects of our technology.

Our success and ability to compete depend to a significant degree upon the protection of our proprietary technology. We currently have two U.S. patents that have been issued to us and four U.S. patent applications that are pending. We may seek additional patents in the future. Our current patent applications cover different aspects of the technology used in our products which is important to our ability to compete. However, it is possible that:

our pending patent applications may not result in the issuance of patents;

any patents acquired by or issued to us may not be broad enough to protect us;

any issued patent could be successfully challenged by one or more third parties, which could result in our loss of the right to prevent others from exploiting the inventions claimed in those patents;

current and future competitors may independently develop similar technology, duplicate our services or design around any of our patents; and

effective patent protection, including effective legal-enforcement mechanisms against those who violate our patent-related assets, may not be available in every country in which we do or plan to do business.

We also rely upon trademarks, copyrights and trade secrets to protect our technology, which may not be sufficient to protect our intellectual property.

We also rely on a combination of laws, such as copyright, trademark and trade secret laws, and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our technology. We have registered seven U.S. and four foreign country trademarks. These forms of intellectual property protection are critically important to our ability to establish and maintain our competitive position. However,

third parties may infringe or misappropriate our copyrights, trademarks and similar proprietary rights;

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laws and contractual restrictions may not be sufficient to prevent misappropriation of our technology or to deter others from developing similar technologies;

effective trademark, copyright and trade secret protection, including effective legal-enforcement mechanisms against those who violate our trademark, copyright or trade secret assets, may be unavailable or limited in foreign countries;

other companies may claim common law trademark rights based upon state or foreign laws that precede the federal registration of our marks; and

policing unauthorized use of our services and trademarks is difficult, expensive and time-consuming, and we may be unable to determine the extent of any unauthorized use.

Reverse engineering, unauthorized copying or other misappropriation of our proprietary technology could enable third parties to benefit from our technology without paying us for it, which would significantly harm our business.

If other parties bring infringement or other claims against us, we may incur significant costs or lose customers.

Other companies may obtain patents or other proprietary rights that would limit our ability to conduct our business and could assert that our technologies infringe their proprietary rights. We could incur substantial costs to defend any legal proceedings, even if without merit, and intellectual property litigation could force us to cease using key technology, obtain a license, or redesign our products. In the course of our business, we may sell certain systems to our customers, and in connection with such sale, we may agree

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to indemnify these customers from claims made against them by third parties for patent infringement related to these systems. In particular, claims are currently being made by holders of patents against educational institutions using streaming in their curriculum. We could be subject to similar claims, which could harm our business.

If we lose key personnel or fail to integrate replacement personnel successfully, our ability to manage our business could be impaired.

Our future success depends upon the continued service of our key management, technical, sales, and other critical personnel. Certain of our officers and certain of our other key personnel are employees-at-will, and we cannot assure that we will be able to retain them. Key personnel have left our company in the past, sometimes to accept employment with companies that sell similar products or services to existing or potential customers of ours. There will likely be additional departures of key personnel from time to time in the future and such departures could result in additional competition, loss of customers or confusion in the marketplace. The loss of any key employee could result in significant disruptions to our operations, including adversely affecting the timeliness of product releases, the successful implementation and completion of company initiatives, and the results of our operations. In particular, the loss of the services of our Chief Executive Officer, Rimas Buinevicius, or our co-founder and Chief Technology Officer, Monty Schmidt, would harm our business. Although we do have employment agreements with Messrs. Buinevicius and Schmidt, we do not have life insurance policies on any of our key employees. In addition, the integration of replacement personnel could be time consuming, may cause disruptions to our operations, and may be unsuccessful.

Because our business is susceptible to risks associated with international operations, we may not be able to maintain or increase international sales of our products.

International product and service billings ranged from 14% to 28% of our total billings in each of the past three years. Our international operations are expected to continue to account for a significant portion of our business in the future. However, in the future we may be unable to maintain or increase international sales of our products and services. International sales are subject to a variety of risks, including:

difficulties in establishing and managing international distribution channels;

difficulties in selling, servicing and supporting overseas products and in translating products into foreign languages;

the uncertainty of laws and enforcement in certain countries relating to the protection of intellectual property or requirements for product certification or other restrictions;

multiple and possibly overlapping tax structures;

currency and exchange rate fluctuations; and

economic or political changes in international markets.

We face risks associated with government regulation of the internet, and related legal uncertainties.

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Currently, few existing laws or regulations specifically apply to the Internet, other than laws generally applicable to businesses. Many Internet-related laws and regulations, however, are pending and may be adopted in the United States, in individual states and local jurisdictions and in other countries. These laws may relate to many areas that impact our business, including encryption, network and information security, and the convergence of traditional communication services, such as telephone services, with Internet communications, taxes and wireless networks. These types of regulations could differ between countries and other political and geographic divisions both inside and outside the United States. Non-U.S. countries and political organizations may impose, or favor, more and different regulation than that which has been proposed in the United States, thus furthering the complexity of regulation. In addition, state and local governments within the United States may impose regulations in addition to, inconsistent with, or stricter than federal regulations. The adoption of such laws or regulations, and uncertainties associated with their validity, interpretation, applicability and enforcement, may affect the available distribution channels for, and the costs associated with, our products and services. The adoption of such laws and regulations may harm our business.

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Exercise of outstanding options and warrants will result in further dilution.

The issuance of shares of common stock upon the exercise of our outstanding options and warrants will result in dilution to the interests of our stockholders, and may reduce the trading price of our common stock.

At September 30, 2009, we had 500 thousand of outstanding warrants and 7.7 million of outstanding stock options granted under our stock option plans, 4.7 million of which are immediately exercisable.

To the extent that these stock options or warrants are exercised, dilution to the interests of our stockholders will likely occur. Additional options and warrants may be issued in the future at prices not less than 85% of the fair market value of the underlying security on the date of grant. Exercises of these options or warrants, or even the potential of their exercise may have an adverse effect on the trading price of our common stock. The holders of our options or our warrants are likely to exercise them at times when the market price of the common stock exceeds the exercise price of the securities. Accordingly, the issuance of shares of common stock upon exercise of the options and warrants will likely result in dilution of the equity represented by the then outstanding shares of common stock held by other stockholders. Holders of our options and warrants can be expected to exercise or convert them at a time when we would, in all likelihood, be able to obtain any needed capital on terms, which are more favorable to us than the exercise terms provided, by these options and warrants.

We may need to make acquisitions or form strategic alliances or partnerships in order to remain competitive in our market, and potential future acquisitions, strategic alliances or partnerships could be difficult to integrate, disrupt our business and dilute stockholder value.

We may acquire or form strategic alliances or partnerships with other businesses in the future in order to remain competitive or to acquire new technologies. As a result of these acquisitions, strategic alliances or partnerships, we may need to integrate products, technologies, widely dispersed operations and distinct corporate cultures. The products, services or technologies of the acquired companies may need to be altered or redesigned in order to be made compatible with our software products and services, or