

Nuance Communications, Inc.
Form 10-K
November 29, 2012

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 year ended September 30, 2012

OR
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934
For the transition period from to

Commission file number 0-27038

NUANCE COMMUNICATIONS, INC.
(Exact name of Registrant as Specified in its Charter)
Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

94-3156479
(I.R.S. Employer
Identification No.)

1 Wayside Road
Burlington, Massachusetts
(Address of Principal Executive Offices)

01803
(Zip Code)

Registrant's telephone number, including area code:
(781) 565-5000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of Each Exchange on Which Registered
Common stock, \$0.001 par value	NASDAQ Stock Market LLC

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

None

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 Section 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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

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company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

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

The aggregate market value of the outstanding common equity held by non-affiliates of the Registrant as of the last business day of the Registrant’s most recently completed second fiscal quarter was approximately \$5.3 billion based upon the last reported sales price on the Nasdaq National Market for such date. For purposes of this disclosure, shares of Common Stock held by officers and directors of the Registrant and by persons who hold more than 5% of the outstanding Common Stock have been excluded because such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily conclusive.

The number of shares of the Registrant’s Common Stock, outstanding as of October 31, 2012, was 312,423,563.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant’s definitive Proxy Statement to be delivered to stockholders in connection with the Registrant’s 2013 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K.

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PART I

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve risks, uncertainties and assumptions that, if they never materialize or if they prove incorrect, could cause our consolidated results to differ materially from those expressed or implied by such forward-looking statements. All statements other than statements of historical fact are statements that could be deemed forward-looking, including statements pertaining to: our future revenue, cost of revenue, research and development expense, selling, general and administrative expenses, amortization of intangible assets and gross margin, earnings, cash flows and liquidity; our strategy relating to our segments; the potential of future product releases; our product development plans and investments in research and development; future acquisitions and anticipated benefits from acquisitions; international operations and localized versions of our products; our contractual commitments; our fiscal 2013 revenue and expense expectations and legal proceedings and litigation matters. You can identify these and other forward-looking statements by the use of words such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “intends,” “potential,” “continue” or the negative of such terms, or other comparable terminology. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth in Item 1A of this Annual Report under the heading “Risk Factors.” All forward-looking statements included in this document are based on information available to us on the date hereof. We will not undertake and specifically decline any obligation to update any forward-looking statements.

Item 1. Business

Overview

We are a leading provider of voice and language solutions for businesses and consumers around the world. Our solutions are used in healthcare, mobile, consumer, enterprise customer service, and imaging markets. We offer market-leading accuracy, natural language understanding capability, domain knowledge and implementation capabilities, built on our significant, long-term investments in research and development. Our solutions are based on our proprietary voice and language platform and are used every day by millions of people and thousands of businesses for tasks and services such as requesting information from a phone-based self-service solution, dictating medical records, searching the mobile Web by voice, entering a destination into a navigation system, or working with PDF documents. We offer our solutions to our customers in a variety of ways, including through products, hosting, professional services and maintenance and support. Our product revenues include embedded original equipment manufacturers (“OEM”) royalties, traditional enterprise licensing, term-based enterprise licensing and consumer-based sales. Our hosting revenues are primarily generated through on-demand service models, comprised of hosted transaction-based pricing arrangements that typically have multi-year terms. Hosting and maintenance and support revenues are recurring in nature as our customers need to use our products on a repeat basis to handle their needs in medical transcription, enterprise customer service and mobile connected services.

We leverage our global professional services organization and our extensive network of partners to design, develop and deploy innovative solutions for businesses and organizations around the globe. We market and sell our products directly through a dedicated sales force, through our e-commerce website and also through a global network of resellers, including system integrators, independent software vendors, value-added resellers, hardware vendors, telecommunications carriers and distributors.

We have built a world-class portfolio of intellectual property, technologies, applications and solutions through both internal development and acquisitions. We expect to continue to pursue opportunities to expand our assets, geographic presence, distribution network and customer base through acquisitions of other businesses and technologies.

We are organized in four segments: Healthcare, Mobile and Consumer, Enterprise, and Imaging. We leverage our voice and language platform to deliver custom, domain-specific solutions across these four segments. In fiscal 2012, segment revenue as a percentage of total segment revenue for Healthcare, Mobile and Consumer, Enterprise and Imaging was 39%, 29%, 19% and 13%, respectively. In fiscal 2011, segment revenue as a percentage of total segment revenue for Healthcare, Mobile and Consumer, Enterprise and Imaging was 38%, 28%, 21% and 13%, respectively. See Note 22 to the consolidated financial statements for additional information about our reportable segments.

Healthcare

The healthcare industry is under significant pressure to streamline operations, reduce costs and improve patient care. In recent years, healthcare organizations such as hospitals, clinics, medical groups, physicians' offices and insurance providers have increasingly turned to improving their clinical documentation process from capturing the physician voice to creating documentation through the use of the information to improve the delivery of care, quality measures, coding accuracy and appropriate reimbursement.

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We provide comprehensive dictation and transcription solutions and services that capture the patient encounters with their physician. These hosted and on-premise solutions provide platforms to generate and distribute clinical documentation through the use of advanced dictation and transcription features, and allow us to deliver scalable, highly productive medical transcription solutions. Additionally, we offer solutions that leverage the captured information and, with state-of-the-art coding, compliance and record management, which streamlines Healthcare Information Management ("HIM") processes to drive compliance and reimbursement. Through Clinical Documentation Improvement ("CDI") programs, we assist in bridging the gap between physicians and coders.

We are uniquely positioned to accelerate future innovation to transform the entire process of clinical documentation, as we are deeply entrenched in the physician base with our voice capture solutions and have the ability to leverage our Clinical Language Understanding technology to power clinical, coder and CDI specialist solutions that intelligently bridge documentation, CDI, coding and compliance. As many physicians adopt mobile devices, we migrate to mobile and cloud based solutions, supporting our transcription solutions as well as solutions that could be easily integrated by independent software vendors in to their mobile electronic health record clients. These solutions will significantly streamline speed and completeness of documentation so that providers can shorten the time between the patient visit and the payment for that visit.

We utilize a focused, enterprise sales team and professional services organization to address the market and implementation requirements of the healthcare industry. Direct distribution is supplemented by distributors and partnerships with electronic medical records application and other healthcare IT providers including, but not limited to Allscripts, Cerner, Epic, GE, IBM, McKesson and the University of Pittsburgh Medical Center ("UPMC"). In some cases, our healthcare solutions are priced under a traditional software perpetual licensing model. However, certain of our healthcare solutions, in particular our transcription solution, are also offered on an on-demand model and priced by volume of usage (such as number of lines transcribed). We continue to experience an increased preference for on-demand pricing model. Representative customers include Advocate, Banner Health, Cleveland Clinic, Department of Veterans Affairs, HCA, Leahy Clinic, Kaiser Permanente, Mayo Clinic, NHS, Providence Health & Services, Sharp, Steward Sutter Health, Tenet, UPMC, U.S. Army and Wellspan.

Mobile and Consumer

We help consumers use the powerful capabilities of their phones, cars, tablets, desktop and portable computers, personal navigation devices and other consumer electronics by enabling the use of voice commands, text-to-speech and enhanced text input solutions to control and interact with these devices more easily and naturally, and to access the array of content and services available on the Internet. Our suite of Dragon general purpose desktop and portable computer dictation applications increases productivity by using speech to create documents, streamline repetitive and complex tasks, input data, complete forms and automate manual transcription processes. Today, an increasing number of people worldwide rely on mobile devices to stay connected, informed and productive. Our suite of mobile solutions and services provides a platform to build, implement and deploy custom solutions on a variety of mobile devices and other consumer electronics. We have focused in recent quarters on integrating our Dragon technology and brand initiatives across mobile and consumer markets.

Our portfolio of mobile and consumer solutions and services includes an integrated suite of voice control and text-to-speech solutions, dictation applications, predictive text technologies, mobile messaging services and emerging services such as dictation, Web search and voicemail-to-text. We utilize a focused, enterprise sales team and professional services organization to address market and implementation requirements. We utilize direct distribution, supplemented by partnerships with electronics suppliers and integrators such as Clarion, Harman Kardon and Rovi. Our solutions are used by mobile phone, automotive, personal navigation device, computer, television and other consumer electronic manufacturers and their suppliers, including Amazon, Apple, Audi, BMW, Ford, Garmin, GM,

HTC, Intel, LG Electronics, Mercedes Benz, Nintendo, Nokia, Panasonic, Samsung, Sharp, T-Mobile, TomTom and Toyota. Telecommunications carriers, web search companies and content providers are increasingly using our mobile search and communication solutions to offer value-added services to their subscribers and customers. Our embedded mobile solutions are sold to automobile and device manufacturers, generally on a royalty model priced per device sold, as well as on a volume of usage model and sometimes on a license model. Our connected mobile services are sold through telecommunications carriers, voicemail system providers, smartphone application developers or directly to consumers, and generally priced on a volume of usage model (such as per subscriber or per use). At the end of fiscal 2012, our mobile cloud services powered handsets, cars, televisions and other mobile devices in 34 languages. Representative connected services customers and partners include Cisco, Comcast, Esnatech, Mitel, Rogers, Siemens, Telefonica, Telstra, Time Warner Cable, TISA, T-Mobile and Vodafone. In addition, various smartphone application stores include hundreds of applications that utilize our technology, such as our Dragon Mobile Assistant, DragonDictation, DragonGo! and FlexT9, as well as third party applications including Amazon Price Check, Ask, Bon' App, Coupons.com, E*Trade, Grainger, Kraft, Merriam-Webster, On-Star, PlaySay, Recipe.com, Snapguide, Target, Vocre and Yellow Pages.

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During the fourth quarter of fiscal 2012, we shipped new versions of Dragon NaturallySpeaking for Windows and Dragon Dictate for Mac, which are currently available in eight languages. Our desktop and portable computer dictation solutions are generally sold under a traditional perpetual software license model. We utilize a combination of our global reseller network and direct sales to distribute our desktop and portable computer dictation products. Resellers include retailers such as Amazon, Best Buy and WalMart. Enterprise customers include organizations such as law firms, insurance agencies and government agencies. Representative customers include ATF, Exxon, FBI, IBM, Texas Department of Family Protective Services and Zurich.

Enterprise

To remain competitive, organizations must improve the quality of customer care while reducing costs and ensuring a positive customer experience. Technological innovation, competitive pressures and rapid commoditization have made it increasingly important for organizations to achieve enduring market differentiation and secure customer loyalty. In this environment, organizations need to satisfy the expectations of increasingly savvy and mobile consumers who demand high levels of customer service.

We deliver a portfolio of customer service business intelligence and authentication solutions that are designed to help companies better support, understand and communicate with their customers. Our solutions include the use of technologies such as speech recognition, natural language understanding, text-to-speech, biometric voice identification and analytics to automate caller identification and authorization, virtual assistants, call steering, completion of tasks such as updates, purchases and information retrieval, and automated outbound notifications. Our solutions improve the customer experience, increase the use of self-service and enable new revenue opportunities. We complement our solutions and products with a global professional services organization that supports customers and partners with business and systems consulting project management, user-interface design, voice science, application development and business performance optimization, allowing us to deliver end-to-end speech solutions and system integration for voice-enabled customer care. In addition, we offer solutions that can meet customer care needs through web sites and direct interaction with applications on cell phones, enabling customers to very quickly retrieve relevant information. Use of our voice and language processing-enabled web sites and mobile customer care solutions can dramatically decrease customer care costs, in comparison to calls handled by operators.

Our solutions are used by a wide variety of enterprises in customer-service intensive sectors, including telecommunications, financial services, travel and entertainment, and government. Our speech solutions are designed to serve our global partners and customers and are available in approximately 80 languages and dialects worldwide. In addition to our own sales and professional services teams, we often work closely with industry partners, including Avaya, Cisco and Genesys, that integrate our solutions into their hardware and software platforms. Our enterprise solutions offerings include both a traditional software perpetual licensing model and an on-demand model and are priced by volume of usage (such as number of minutes callers use the system or number of calls completed in the system). Representative customers include Bank of America, Barclays, Cigna, Citibank, Comcast, Deutsche Bank, Disney, FedEx, OnStar, PG&E, U.K.HM Revenue & Customs, USAA, US Airways, Telecom Italia, Telefonica, T-Mobile, Wells Fargo and Verizon.

Imaging

The evolution of the Internet, email and other networks has greatly simplified the ability to share electronic documents, resulting in an ever-growing volume of documents to be used and stored. In addition, the proliferation of network and Internet connected multifunction printers has increased the need to efficiently manage printers and enforce printing policies. Our document imaging, print management and PDF solutions reduce the costs associated with paper documents through easy to use scanning, document management and electronic document routing solutions. We offer versions of our products to multifunction printer manufacturers, home offices, small businesses

and enterprise customers.

Our imaging solutions offer optical character recognition technology to deliver highly accurate document scanning and storage. We provide networked print management and comprehensive PDF applications designed specifically for business users. In addition, we offer applications that combine network scanning, network print management and PDF creation to quickly enable distribution of documents to users' desktops or to enterprise applications. Our host of services includes software development toolkits for independent software vendors. Our imaging solutions are generally sold under a traditional perpetual software license model, and some solutions are also offered as a hosted solution. We utilize a combination of our global reseller network and direct sales to distribute our imaging products. We license our software to multifunction printer manufacturers such as Brother, Canon, Dell, HP and Xerox, which bundle our solutions with multi-function devices, digital copiers, printers and scanners, on a royalty model, priced per unit sold. Representative customers include Aflac, Airbus, Amazon, Barclays, Blue Shield, Citibank, EMC, Ernst & Young, Eurostar, Franklin Templeton, Intuit, Johnson & Johnson, JP Morgan Chase, Nationwide, Norwegian Tax Authorities, Office Depot, Phillips, PricewaterhouseCoopers, UPS and US Department of Justice.

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Research and Development/Intellectual Property

In recent years, we have developed and acquired extensive technology assets, intellectual property and industry expertise in voice, language and imaging that provide us with a competitive advantage in our markets. Our technologies are based on complex algorithms which require extensive amounts of linguistic and image data, acoustic models and recognition techniques. A significant investment in capital and time would be necessary to replicate our current capabilities.

We continue to invest in technologies to maintain our market-leading position and to develop new applications. Our technologies are covered by approximately 2,800 patents and 1,100 patent applications. Our intellectual property, whether purchased or developed internally, is critical to our success and competitive position and, ultimately, to our market value. We rely on a portfolio of patents, copyrights, trademarks, services marks, trade secrets, confidentiality provisions and licensing arrangements to establish and protect our intellectual property and proprietary rights. We incurred research and development expenses of \$225.4 million, \$179.4 million, and \$152.1 million in fiscal 2012, 2011 and 2010, respectively.

International Operations

We have principal offices in a number of international locations including: Australia, Belgium, Canada, Germany, Hungary, India, Ireland, Italy, Japan, and the United Kingdom. The responsibilities of our international operations include research and development, healthcare transcription and editing, customer support, sales and marketing and administration. Additionally, we maintain smaller sales, services and support offices throughout the world to support our international customers and to expand international revenue opportunities.

Geographic revenue classification is based on the geographic areas in which our customers are located. For fiscal 2012, 2011 and 2010, 71%, 73% and 72% of revenue was generated in the United States and 29%, 27% and 28% of revenue was generated by our international operations, respectively.

Competition

The individual markets in which we compete are highly competitive and are subject to rapid technology changes. There are a number of companies that develop or may develop products that compete in our target markets; however, currently there is no one company that competes with us in all of our product areas. While we expect competition to continue to increase both from existing competitors and new market entrants, we believe that we will compete effectively based on many factors, including:

Specialized Professional Services. Our superior technology, when coupled with the high quality and domain knowledge of our professional services organization, allows our customers and partners to place a high degree of confidence and trust in our ability to deliver results. We support our customers in designing and building powerful innovative applications that specifically address their needs and requirements.

International Appeal. The international reach of our products is due to the broad language coverage of our offerings, including our voice and language technology, which provides recognition for approximately 80 languages and dialects and natural-sounding synthesized speech in 65 languages, and supports a broad range of hardware platforms and operating systems. Our imaging technology supports more than 100 languages for Optical Character Recognition and document handling, with up to 20 screen language choices, including Asian languages.

Technological Superiority. Our voice, language and imaging technologies, applications and solutions are often recognized as the most innovative and proficient products in their respective categories. Our voice and language technology has industry-leading recognition accuracy and provides a natural, voice-enabled interaction with systems, devices and applications. Our imaging technology is viewed as the most accurate in the industry. Technology

publications, analyst research and independent benchmarks have consistently indicated that our products rank at or above performance levels of alternative solutions.

Broad Distribution Channels. Our ability to address the needs of specific markets, such as financial, legal, healthcare and government, and to introduce new products and solutions quickly and effectively is enhanced through our dedicated direct sales force; our extensive global network of resellers, comprising system integrators, independent software vendors, value-added resellers, hardware vendors, telecommunications carriers and distributors; and our e-commerce website (www.nuance.com).

In our segments, we compete with companies such as Adobe, M*Modal, Microsoft and Google. In addition, a number of smaller companies in both speech and imaging offer services, technologies or products that are competitive with our solutions in some markets. In certain markets, some of our partners such as Avaya, Cisco, Interville and Genesys develop and market products

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and services that might be considered substitutes for our solutions. Current and potential competitors have established, or may establish, cooperative relationships among themselves or with third parties to increase the ability of their technologies to address the needs of our prospective customers.

Some of our competitors or potential competitors, such as Adobe, Microsoft and Google, have significantly greater financial, technical and marketing resources than we do. These competitors may be able to respond more rapidly than we can to new or emerging technologies or changes in customer requirements. They may also devote greater resources to the development, promotion and sale of their products than we do.

Employees

As of September 30, 2012, we had approximately 12,000 full-time employees in total, including approximately 1,000 in sales and marketing, approximately 2,000 in professional services, approximately 1,500 in research and development, approximately 800 in general and administrative and approximately 6,700 that provide transcription and editing services. Approximately 37 percent of our employees are based outside of the United States, the majority of whom provide transcription and editing services and are based in India. Our employees are not represented by any labor union and are not organized under a collective bargaining agreement, and we have never experienced a work stoppage. We believe that our relationships with our employees are generally good.

Company Information

We were incorporated in 1992 as Visioneer, Inc. under the laws of the state of Delaware. In 1999, we changed our name to ScanSoft, Inc. and also changed our ticker symbol to SSFT. In October 2005, we changed our name to Nuance Communications, Inc. and in November 2005 we changed our ticker symbol to NUAN.

Our website is located at www.nuance.com. This Annual Report on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K, and all amendments to these reports, as well as proxy statements and other information we file with or furnish to the Securities and Exchange Commission, or the SEC, are accessible free of charge on our website. We make these documents available as soon as reasonably practicable after we file them with, or furnish them to, the SEC. Our SEC filings are also available on the SEC's website at <http://www.sec.gov>. Alternatively, you may access any document we have filed by visiting the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. Except as otherwise stated in these documents, the information contained on our website or available by hyperlink from our website is not incorporated by reference into this report or any other documents we file with or furnish to the SEC.

Item 1A. Risk Factors

You should carefully consider the risks described below when evaluating our company and when deciding whether to invest in our company. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we do not currently believe are important to an investor may also harm our business operations. If any of the events, contingencies, circumstances or conditions described in the following risks actually occurs, our business, financial condition or our results of operations could be seriously harmed. If that happens, the trading price of our common stock could decline and you may lose part or all of the value of any of our shares held by you.

Risks Related to Our Business

Our operating results may fluctuate significantly from period to period, and this may cause our stock price to decline.

Our revenue and operating results have fluctuated in the past and are expected to continue to fluctuate in the future. Given this fluctuation, we believe that quarter to quarter comparisons of revenue and operating results are not necessarily meaningful or an accurate indicator of our future performance. As a result, our results of operations may not meet the expectations of securities analysts or investors in the future. If this occurs, the price of our stock would likely decline. Factors that contribute to fluctuations in operating results include the following:

- slowing sales by our distribution and fulfillment partners to their customers, which may place pressure on these partners to reduce purchases of our products;
- volume, timing and fulfillment of customer orders;
- our ability to generate additional revenue from our intellectual property portfolio;

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customers delaying their purchasing decisions in anticipation of new versions of our products;
customers delaying, canceling or limiting their purchases as a result of the threat or results of terrorism;
introduction of new products by us or our competitors;
seasonality in purchasing patterns of our customers;
reduction in the prices of our products in response to competition, market conditions or contractual obligations;
returns and allowance charges in excess of accrued amounts;
timing of significant marketing and sales promotions;
impairment charges against goodwill and intangible assets;
delayed realization of synergies resulting from our acquisitions;
write-offs of excess or obsolete inventory and accounts receivable that are not collectible;
increased expenditures incurred pursuing new product or market opportunities;
general economic trends as they affect retail and corporate sales; and
higher than anticipated costs related to fixed-price contracts with our customers.

Due to the foregoing factors, among others, our revenue and operating results are difficult to forecast. Our expense levels are based in significant part on our expectations of future revenue and we may not be able to reduce our expenses quickly to respond to a shortfall in projected revenue. Therefore, our failure to meet revenue expectations would seriously harm our operating results, financial condition and cash flows.

We have grown, and may continue to grow, through acquisitions, which could dilute our existing stockholders.

As part of our business strategy, we have in the past acquired, and expect to continue to acquire, other businesses and technologies. In connection with past acquisitions, we issued a substantial number of shares of our common stock as transaction consideration and also incurred significant debt to finance the cash consideration used for our acquisitions.

We may continue to issue equity securities for future acquisitions, which would dilute existing stockholders, perhaps significantly depending on the terms of such acquisitions. We may also incur additional debt in connection with future acquisitions, which, if available at all, may place additional restrictions on our ability to operate our business.

Our ability to realize the anticipated benefits of our acquisitions will depend on successfully integrating the acquired businesses.

Our prior acquisitions required, and our recently completed acquisitions continue to require, substantial integration and management efforts and we expect future acquisitions to require similar efforts. Acquisitions of this nature involve a number of risks, including:

difficulty in transitioning and integrating the operations and personnel of the acquired businesses;
potential disruption of our ongoing business and distraction of management;
potential difficulty in successfully implementing, upgrading and deploying in a timely and effective manner new operational information systems and upgrades of our finance, accounting and product distribution systems;
difficulty in incorporating acquired technology and rights into our products and technology;
potential difficulties in completing projects associated with in-process research and development;
unanticipated expenses and delays in completing acquired development projects and technology integration;
management of geographically remote business units both in the United States and internationally;
impairment of relationships with partners and customers;
assumption of unknown material liabilities of acquired companies;
inaccurate projection of revenue plans of the acquired entity in the due diligence process;
customers delaying purchases of our products pending resolution of product integration between our existing and our newly acquired products;

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entering markets or types of businesses in which we have limited experience; and
potential loss of key employees of the acquired business.

As a result of these and other risks, if we are unable to successfully integrate acquired businesses, we may not realize the anticipated benefits from our acquisitions. Any failure to achieve these benefits or failure to successfully integrate acquired businesses and technologies could seriously harm our business.

Charges to earnings as a result of our acquisitions may adversely affect our operating results in the foreseeable future, which could have a material and adverse effect on the market value of our common stock.

Under accounting principles generally accepted in the United States of America, we record the market value of our common stock or other form of consideration issued in connection with an acquisition as the cost of acquiring the company or business. We have allocated that cost to the individual assets acquired and liabilities assumed, including various identifiable intangible assets such as acquired technology, acquired trade names and acquired customer relationships based on their respective fair values. Our estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain. After we complete an acquisition, the following factors could result in material charges and adversely affect our operating results and may adversely affect our cash flows:

- costs incurred to combine the operations of businesses we acquire, such as transitional employee expenses and employee retention, redeployment or relocation expenses;

- impairment of goodwill or intangible assets;

- amortization of intangible assets acquired;

- a reduction in the useful lives of intangible asset acquired;

- identification of or changes to assumed contingent liabilities, both income tax and non-income tax related after our final determination of the amounts for these contingencies or the conclusion of the measurement period (generally up to one year from the acquisition date), whichever comes first;

- charges to our operating results to eliminate certain duplicative pre-merger activities, to restructure our operations or to reduce our cost structure;

- charges to our operating results resulting from expenses incurred to effect the acquisition; and

- charges to our operating results due to the expensing of certain stock awards assumed in an acquisition.

Intangible assets are generally amortized over a five to fifteen year period. Goodwill and certain intangible assets with indefinite lives, are not subject to amortization but are subject to an impairment analysis, at least annually, which may result in an impairment charge if the carrying value exceeds its implied fair value. As of September 30, 2012, we had identified intangible assets of approximately \$906.5 million, net of accumulated amortization, and goodwill of approximately \$3.0 billion. In addition, purchase accounting limits our ability to recognize certain revenue that otherwise would have been recognized by the acquired company as an independent business. As a result, the combined company may delay revenue recognition or recognize less revenue than we and the acquired company would have recognized as independent companies.

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Our significant debt could adversely affect our financial health and prevent us from fulfilling our obligations under our credit facility and our convertible debentures.

We have a significant amount of debt. As of September 30, 2012, we had a total of \$2,270.7 million of gross debt outstanding, including \$143.5 million in term loans due in March 2013, \$487.1 million in term loans due in March 2016 under an amended and restated agreement signed in July 2011, \$700.0 million of senior notes due in 2020 and \$940.0 million in convertible debentures. In October, 2012, we issued \$350.0 million of senior notes due in 2020 and used \$143.5 million of the proceeds to prepay the term loans due in March 2013. Investors may require us to redeem the 2027 Debentures totaling \$250.0 million in aggregate principal amount in August 2014, or sooner if the closing sale price of our common stock is more than 120% of the then current conversion price for certain specified periods. If a holder elects to convert, we will be required to pay the principal amount in cash and any amounts payable in excess of the principal amount will be paid in cash or shares of our common stock, at our election. Investors may require us to redeem the 2031 Debentures, totaling \$690.0 million in aggregate principal amount in November 2017, or sooner if the closing sale price of our common stock is more than 130% of the then current conversion price for certain specified periods. If a holder elects to convert, we will be required to pay the principal amount in cash and any amounts payable in excess of the principal amount will be paid in cash or shares of our common stock, at our election. We also have a \$75.0 million revolving credit line available to us through March 2015. As of September 30, 2012, there were \$17.9 million of letters of credit issued, but there were no other outstanding borrowings under the revolving credit line. Our debt level could have important consequences, for example it could:

- require us to use a large portion of our cash flow to pay principal and interest on debt, including the convertible debentures and the credit facility, which will reduce the availability of our cash flow to fund working capital, capital expenditures, acquisitions, research and development expenditures and other business activities;
- restrict us from making strategic acquisitions or exploiting business opportunities;
- place us at a competitive disadvantage compared to our competitors that have less debt; and
- limit, along with the financial and other restrictive covenants related to our debt, our ability to borrow additional funds, dispose of assets or pay cash dividends.

Our ability to meet our payment and other obligations under our debt instruments depends on our ability to generate significant cash flow in the future. This, to some extent, is subject to general economic, financial, competitive, legislative and regulatory factors as well as other factors that are beyond our control. We cannot assure you that our business will generate cash flow from operations, or that additional capital will be available to us, in an amount sufficient to enable us to meet our payment obligations under the convertible debentures and our other debt and to fund other liquidity needs. If we are not able to generate sufficient cash flow to service our debt obligations, we may need to refinance or restructure our debt, including the convertible debentures, sell assets, reduce or delay capital investments, or seek to raise additional capital. If we are unable to implement one or more of these alternatives, we may not be able to meet our payment obligations under the convertible debentures and our other debt.

In addition, approximately \$630.6 million of our debt outstanding as of September 30, 2012 bears interest at variable rates. If market interest rates increase, our debt service requirements will increase, which would adversely affect our results of operations and cash flows.

Our debt agreements contain covenant restrictions that may limit our ability to operate our business.

The agreement governing our senior credit facility contains, and any of our other future debt agreements may contain, covenant restrictions that limit our ability to operate our business, including restrictions on our ability to:

- incur additional debt or issue guarantees;
- create liens;
- make certain investments;
- enter into transactions with our affiliates;
- sell certain assets;
- redeem capital stock or make other restricted payments;
- declare or pay dividends or make other distributions to stockholders; and
- merge or consolidate with any entity.

Our ability to comply with these covenants is dependent on our future performance, which will be subject to many factors, some of which are beyond our control, including prevailing economic conditions. As a result of these covenants, our ability to respond to changes in business and economic conditions and to obtain additional financing, if needed, may be significantly

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restricted, and we may be prevented from engaging in transactions that might otherwise be beneficial to us. In addition, our failure to comply with these covenants could result in a default under our debt agreements, which could permit the holders to accelerate our obligation to repay the debt. If any of our debt is accelerated, we may not have sufficient funds available to repay the accelerated debt.

We have a history of operating losses, and may incur losses in the future, which may require us to raise additional capital on unfavorable terms.

We reported net income of \$207.1 million and \$38.2 million in fiscal 2012 and 2011, respectively, net losses of \$19.1 million for the fiscal year 2010 and have a total accumulated deficit of \$161.2 million as of September 30, 2012. If we are unable to maintain profitability, the market price for our stock may decline, perhaps substantially. We cannot assure you that our revenue will grow or that we will maintain profitability in the future. If we do not achieve and maintain profitability, we may be required to raise additional capital to maintain or grow our operations. Additional capital, if available at all, may be highly dilutive to existing investors or contain other unfavorable terms, such as a high interest rate and restrictive covenants.

Voice and language technologies may not continue to garner widespread acceptance, which could limit our ability to grow our voice and language business.

We have invested and expect to continue to invest heavily in the acquisition, development and marketing of voice and language technologies. The market for voice and language technologies is relatively new and rapidly evolving. Our ability to increase revenue in the future depends in large measure on the continuing acceptance of these technologies in general and our products in particular. The continued development of the market for our current and future voice and language solutions in general, and our solutions in particular, will also depend on:

- consumer and business demand for speech-enabled applications;
- development by third-party vendors of applications using voice and language technologies; and
- continuous improvement in voice and language technology.

Sales of our voice and language products would be harmed if the market for these technologies does not continue to increase or increases slower than we expect, or if we fail to develop new technology faster than our competitors, and consequently, our business could be harmed and we may not achieve a level of profitability necessary to successfully operate our business.

The markets in which we operate are highly competitive and rapidly changing and we may be unable to compete successfully.

There are a number of companies that develop or may develop products that compete in our targeted markets. The individual markets in which we compete are highly competitive, and are rapidly changing. Within voice and language, we compete with AT&T, Google, Microsoft, and other smaller providers. Within healthcare, we compete with M*Modal and other smaller providers. Within imaging, we compete with ABBYY, Adobe, I.R.I.S. and NewSoft. In voice and language, some of our partners such as Avaya, Cisco, Intervoice and Genesys develop and market products that can be considered substitutes for our solutions. In addition, a number of smaller companies in voice, language and imaging produce technologies or products that are in some markets competitive with our solutions. Current and potential competitors have established, or may establish, cooperative relationships among themselves or with third parties to increase the ability of their technologies to address the needs of our prospective customers.

The competition in these markets could adversely affect our operating results by reducing the volume of the products we license or the prices we can charge. Some of our current or potential competitors, such as Adobe, Google and Microsoft, have significantly greater financial, technical and marketing resources than we do. These competitors may be able to respond more rapidly than we can to new or emerging technologies or changes in customer requirements. They may also devote greater resources to the development, promotion and sale of their products than we do.

Some of our customers, such as Google and Microsoft, have developed or acquired products or technologies that compete with our products and technologies. These customers may give higher priority to the sale of these competitive products or technologies. To the extent they do so, market acceptance and penetration of our products, and therefore our revenue, may be adversely affected. Our success will depend substantially upon our ability to enhance our products and technologies and to develop and introduce, on a timely and cost-effective basis, new products and features that meet changing customer requirements and incorporate technological enhancements. If we

are unable to develop new products and enhance functionalities or technologies to adapt to these changes, or if we are unable to realize synergies among our acquired products and technologies, our business will suffer.

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The failure to successfully maintain the adequacy of our system of internal control over financial reporting could have a material adverse impact on our ability to report our financial results in an accurate and timely manner.

The SEC, as directed by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring public companies to include a report of management on internal control over financial reporting in their annual reports on Form 10-K that contains an assessment by management of the effectiveness of our internal control over financial reporting. In addition, our independent registered public accounting firm must attest to and report on the effectiveness of our internal control over financial reporting. Any failure in the effectiveness of our system of internal control over financial reporting could have a material adverse impact on our ability to report our financial statements in an accurate and timely manner, could subject us to regulatory actions, civil or criminal penalties, shareholder litigation, or loss of customer confidence, which could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements, which ultimately could negatively impact our stock price.

A significant portion of our revenue is derived, and a significant portion of our research and development activities are based, outside the United States. Our results could be harmed by economic, political, regulatory and other risks associated with these international regions.

Because we operate worldwide, our business is subject to risks associated with doing business internationally. We anticipate that revenue from international operations could increase in the future. Most of our international revenue is generated by sales in Europe and Asia. In addition, some of our products are developed and manufactured outside the United States and we have a large number of employees in India that provide transcription services. We also have a large number of employees in Canada, Germany and United Kingdom that provide professional services. A significant portion of the development of our voice and language products is conducted in Canada and Germany, and a significant portion of our imaging research and development is conducted in Hungary. We also have significant research and development resources in Austria, Belgium, Italy, and United Kingdom. Accordingly, our future results could be harmed by a variety of factors associated with international sales and operations, including:

- changes in a specific country's or region's economic conditions;
- geopolitical turmoil, including terrorism and war;
- trade protection measures and import or export licensing requirements imposed by the United States or by other countries;
- compliance with foreign and domestic laws and regulations;
- negative consequences from changes in applicable tax laws;
- difficulties in staffing and managing operations in multiple locations in many countries;
- difficulties in collecting trade accounts receivable in other countries; and
- less effective protection of intellectual property than in the United States.

We are exposed to fluctuations in foreign currency exchange rates.

Because we have international subsidiaries and distributors that operate and sell our products outside the United States, we are exposed to the risk of changes in foreign currency exchange rates. In certain circumstances, we have entered into forward exchange contracts to hedge against foreign currency fluctuations. We use these contracts to reduce our risk associated with exchange rate movements, as the gains or losses on these contracts are intended to offset any exchange rate losses or gains on the hedged transaction. We do not engage in foreign currency speculation. With our increased international presence in a number of geographic locations and with international revenue and costs projected to increase, we are exposed to changes in foreign currencies including the euro, British pound, Canadian dollar, Japanese yen, Indian rupee, Australian dollar, Israeli shekel, Swiss franc and the Hungarian forint. Changes in the value of foreign currencies relative to the value of the U.S. dollar could adversely affect future revenue and operating results.

Impairment of our intangible assets could result in significant charges that would adversely impact our future operating results.

We have significant intangible assets, including goodwill and intangibles with indefinite lives, which are susceptible to valuation adjustments as a result of changes in various factors or conditions. The most significant intangible assets are patents and core technology, completed technology, customer relationships and trademarks. Customer relationships are amortized on an accelerated basis based upon the pattern in which the economic benefits of customer

relationships are being utilized. Other identifiable intangible assets are amortized on a straight-line basis over their estimated useful lives. We assess the potential impairment of intangible assets on an annual basis, as well as whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors that could trigger an impairment of such assets include the following:

- significant underperformance relative to historical or projected future operating results;

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• significant changes in the manner of or use of the acquired assets or the strategy for our overall business;

• significant negative industry or economic trends;

• significant decline in our stock price for a sustained period;

changes in our organization or management reporting structure that could result in additional reporting units, which may require alternative methods of estimating fair values or greater disaggregation or aggregation in our analysis by reporting unit; and

• a decline in our market capitalization below net book value.

Future adverse changes in these or other unforeseeable factors could result in an impairment charge that would impact our results of operations and financial position in the reporting period identified.

Our sales to government clients subject us to risks, including early termination, audits, investigations, sanctions and penalties.

We derive a portion of our revenues from contracts with the United States government, as well as various state and local governments, and their respective agencies. Government contracts are generally subject to audits and investigations which could identify violations of these agreements. Government contract violations could result in a range of consequences including, but not limited to, contract price adjustments, civil and criminal penalties, contract termination, forfeiture of profit and/or suspension of payment, and suspension or debarment from future government contracts. We could also suffer serious harm to our reputation if we were found to have violated the terms of our government contracts.

We conducted an analysis of our compliance with the terms and conditions of certain contracts with the U.S. General Services Administration (“GSA”). Based upon our analysis, we voluntarily notified GSA of non-compliance with the terms of two contracts. The final resolution of this matter may adversely impact our financial position.

If we are unable to attract and retain key personnel, our business could be harmed.

If any of our key employees were to leave, we could face substantial difficulty in hiring qualified successors and could experience a loss in productivity while any successor obtains the necessary training and experience. Our employment relationships are generally at-will and we have had key employees leave in the past. We cannot assure you that one or more key employees will not leave in the future. We intend to continue to hire additional highly qualified personnel, including software engineers and operational personnel, but may not be able to attract, assimilate or retain qualified personnel in the future. Any failure to attract, integrate, motivate and retain these employees could harm our business. Our medical transcription services may be subject to legal claims for failure to comply with laws governing the confidentiality of medical records.

Healthcare professionals who use our medical transcription services deliver to us health information about their patients including information that constitutes a record under applicable law that we may store on our computer systems. Numerous federal and state laws and regulations, the common law and contractual obligations govern collection, dissemination, use and confidentiality of patient-identifiable health information, including:

- state and federal privacy and confidentiality laws;
- our contracts with customers and partners;
- state laws regulating healthcare professionals;
- Medicaid laws; and
- the Health Insurance Portability and Accountability Act of 1996 and related rules proposed by the Health Care Financing Administration.

The Health Insurance Portability and Accountability Act of 1996 establishes elements including, but not limited to, federal privacy and security standards for the use and protection of protected health information. Any failure by us or by our personnel or partners to comply with applicable requirements may result in a material liability. Although we have systems and policies in place for safeguarding protected health information from unauthorized disclosure, these systems and policies may not preclude claims against us for alleged violations of applicable requirements. There can be no assurance that we will not be subject to liability claims that could have a material adverse affect on our business, results of operations and financial condition.

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Adverse changes in general economic or political conditions in any of the major countries in which we do business could adversely affect our operating results.

Adverse changes in domestic and global economic and political conditions, as well as uncertainty in the global financial markets may negatively affect our financial results. These macroeconomic developments could negatively affect our business, operating results or financial condition in a number of ways which, in turn, could adversely affect our stock price. A prolonged period of economic decline could have a material adverse effect on our results of operations and financial condition and exacerbate some of the other risk factors described herein. Our customers may defer purchases of our products, licenses, and services in response to tighter credit and negative financial news or reduce their demand for them. Our customers may also not be able to obtain adequate access to credit, which could affect their ability to make timely payments to us or ultimately cause the customer to file for protection from creditors under applicable insolvency or bankruptcy laws. If our customers are not able to make timely payments to us, our accounts receivable could increase. Political instability in any of the major countries in which we do business would also likely harm our business, results of operations and financial condition.

Current uncertainty in the global financial markets and the global economy may negatively affect our financial results. Our investment portfolio, which primarily includes investments in money market funds, is generally subject to credit, liquidity, counterparty, market and interest rate risks that may be exacerbated by the recent global financial crisis. If the banking system or the fixed income, credit or equity markets deteriorate or remain volatile, our investment portfolio may be impacted and the values and liquidity of our investments could be adversely affected.

In addition, our operating results and financial condition could be negatively affected if, as a result of economic conditions, either:

- the demand for, and prices of, our products, licenses, or services are reduced as a result of actions by our competitors or otherwise; or

- our financial counterparties or other contractual counterparties are unable to, or do not, meet their contractual commitments to us.

Security and privacy breaches in our systems may damage client relations and inhibit our growth.

The uninterrupted operation of our hosted solutions and the confidentiality and security of third-party information is critical to our business. Any failures in our security and privacy measures could have a material adverse effect on our financial position and results of operations. If we are unable to protect, or our clients perceive that we are unable to protect, the security and privacy of our electronic information, our growth could be materially adversely affected. A security or privacy breach may:

- cause our clients to lose confidence in our solutions;

- harm our reputation;

- expose us to liability; and

- increase our expenses from potential remediation costs.

While we believe we use proven applications designed for data security and integrity to process electronic transactions, there can be no assurance that our use of these applications will be sufficient to address changing market conditions or the security and privacy concerns of existing and potential clients.

Interruptions or delays in service from data center hosting facilities could impair the delivery of our service and harm our business.

We currently serve our customers from data center hosting facilities. Any damage to, or failure of, our systems generally could result in interruptions in our service. Interruptions in our service may reduce our revenue, cause us to issue credits or pay penalties, cause customers to terminate their on-demand services and adversely affect our renewal rates and our ability to attract new customers.

Risks Related to Our Intellectual Property and Technology

Unauthorized use of our proprietary technology and intellectual property could adversely affect our business and results of operations.

Our success and competitive position depend in large part on our ability to obtain and maintain intellectual property rights protecting our products and services. We rely on a combination of patents, copyrights, trademarks, service marks, trade secrets, confidentiality provisions and licensing arrangements to establish and protect our intellectual

property and proprietary rights. Unauthorized parties may attempt to copy aspects of our products or to obtain, license, sell or otherwise use information that we

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regard as proprietary. Policing unauthorized use of our products is difficult and we may not be able to protect our technology from unauthorized use. Additionally, our competitors may independently develop technologies that are substantially the same or superior to our technologies and that do not infringe our rights. In these cases, we would be unable to prevent our competitors from selling or licensing these similar or superior technologies. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as the laws of the United States. Although the source code for our proprietary software is protected both as a trade secret and as a copyrighted work, litigation may be necessary to enforce our intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others, or to defend against claims of infringement or invalidity. Litigation, regardless of the outcome, can be very expensive and can divert management efforts. Third parties have claimed and may claim in the future that we are infringing their intellectual property, and we could be exposed to significant litigation or licensing expenses or be prevented from selling our products if such claims are successful.

From time to time, we are subject to claims that we or our customers may be infringing or contributing to the infringement of the intellectual property rights of others. We may be unaware of intellectual property rights of others that may cover some of our technologies and products. If it appears necessary or desirable, we may seek licenses for these intellectual property rights. However, we may not be able to obtain licenses from some or all claimants, the terms of any offered licenses may not be acceptable to us, and we may not be able to resolve disputes without litigation. Any litigation regarding intellectual property could be costly and time-consuming and could divert the attention of our management and key personnel from our business operations. In the event of a claim of intellectual property infringement, we may be required to enter into costly royalty or license agreements. Third parties claiming intellectual property infringement may be able to obtain injunctive or other equitable relief that could effectively block our ability to develop and sell our products.

We may incur substantial costs enforcing or acquiring intellectual property rights and defending against third-party claims as a result of litigation or other proceedings.

In connection with the enforcement of our own intellectual property rights, the acquisition of third-party intellectual property rights, or disputes relating to the validity or alleged infringement of third-party intellectual property rights, including patent rights, we have been, are currently, and may in the future be, subject to claims, negotiations or complex, protracted litigation. Intellectual property disputes and litigation are typically very costly and can be disruptive to our business operations by diverting the attention and energy of management and key technical personnel. Although we have successfully defended or resolved past litigation and disputes, we may not prevail in any ongoing or future litigation and disputes. In addition, we may incur significant costs in acquiring the necessary third party intellectual property rights for use in our products. Third party intellectual property disputes could subject us to significant liabilities, require us to enter into royalty and licensing arrangements on unfavorable terms, prevent us from manufacturing or licensing certain of our products, cause severe disruptions to our operations or the markets in which we compete, or require us to satisfy indemnification commitments with our customers including contractual provisions under various license arrangements. Any of these could seriously harm our business.

Our software products may have bugs, which could result in delayed or lost revenue, expensive correction, liability to our customers and claims against us.

Complex software products such as ours may contain errors, defects or bugs. Defects in the solutions or products that we develop and sell to our customers could require expensive corrections and result in delayed or lost revenue, adverse customer reaction and negative publicity about us or our products and services. Customers who are not satisfied with any of our products may also bring claims against us for damages, which, even if unsuccessful, would likely be time-consuming to defend, and could result in costly litigation and payment of damages. Such claims could harm our reputation, financial results and competitive position.

Risks Related to our Corporate Structure, Organization and Common Stock

The holdings of our largest stockholder may enable it to influence matters requiring stockholder approval.

As of September 30, 2012, Warburg Pincus, a global private equity firm, beneficially owned approximately 17.9% of our outstanding common stock, including 3,562,238 shares of our outstanding Series B Preferred Stock, each of which is convertible into one share of our common stock. Because of its large holdings of our capital stock relative to other

stockholders, this stockholder has a strong influence over matters requiring approval by our stockholders.

The market price of our common stock has been and may continue to be subject to wide fluctuations, and this may make it difficult for you to resell the common stock when you want or at prices you find attractive.

Our stock price historically has been, and may continue to be, volatile. Various factors contribute to the volatility of our stock price, including, for example, quarterly variations in our financial results, new product introductions by us or our competitors

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and general economic and market conditions. Sales of a substantial number of shares of our common stock by our largest stockholders, or the perception that such sales could occur, could also contribute to the volatility of our stock price. While we cannot predict the individual effect that these factors may have on the market price of our common stock, these factors, either individually or in the aggregate, could result in significant volatility in our stock price during any given period of time. Moreover, companies that have experienced volatility in the market price of their stock often are subject to securities class action litigation. If we were the subject of such litigation, it could result in substantial costs and divert management's attention and resources.

Compliance with changing regulation of corporate governance and public disclosure may result in additional expenses.

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, the Dodd-Frank Wall Street Reform and Consumer Protection Act, new regulations promulgated by the Securities and Exchange Commission and the rules of the Nasdaq Marketplace, are resulting in increased general and administrative expenses for companies such as ours. These new or changed laws, regulations and standards are subject to varying interpretations in many cases, and as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies, which could result in higher costs necessitated by ongoing revisions to disclosure and governance practices. We are committed to maintaining high standards of corporate governance and public disclosure. As a result, we intend to invest resources to comply with evolving laws, regulations and standards, and this investment may result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities. If our efforts to comply with new or changed laws, regulations and standards differ from the activities intended by regulatory or governing bodies, our business may be harmed.

Future sales of our common stock in the public market could adversely affect the trading price of our common stock and our ability to raise funds in new stock offerings.

Future sales of substantial amounts of our common stock in the public market, or the perception that such sales could occur, could adversely affect prevailing trading prices of our common stock and could impair our ability to raise capital through future offerings of equity or equity-related securities. In connection with past acquisitions, we issued a substantial number of shares of our common stock as transaction consideration. We may continue to issue equity securities for future acquisitions, which would dilute existing stockholders, perhaps significantly depending on the terms of such acquisitions. No prediction can be made as to the effect, if any, that future sales of shares of common stock, or the availability of shares of common stock for future sale, will have on the trading price of our common stock.

We have implemented anti-takeover provisions, which could discourage or prevent a takeover, even if an acquisition would be beneficial to our stockholders.

Provisions of our certificate of incorporation, bylaws and Delaware law, as well as other organizational documents could make it more difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders.

These provisions include:

- authorized "blank check" preferred stock;
- prohibiting cumulative voting in the election of directors;
- limiting the ability of stockholders to call special meetings of stockholders;
- requiring all stockholder actions to be taken at meetings of our stockholders; and
- establishing advance notice requirements for nominations of directors and for stockholder proposals.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

Our corporate headquarters and administrative, sales, marketing, research and development and customer support functions occupy approximately 234,000 square feet of space that we lease in Burlington, Massachusetts. We also lease additional properties in the United States and a number of foreign countries. The following table summarizes our significant properties as of September 30, 2012:

Location	Sq. Ft. (approx.)	Lease Term	Primary Use
Burlington, Massachusetts	234,000	March, 2018	Corporate headquarters and administrative, sales, marketing, research and development and customer support functions.
Melbourne, Florida	130,000	Owned	Administrative, customer support and professional services functions.
Montreal, Quebec	98,000	December, 2016	Research and development, professional services, customer support functions.
Sunnyvale, California	71,000	September, 2013	Administrative, research and development, professional services and customer support functions.
Bangalore, India	50,000	April, 2015	Transcription and editing services

In addition to the properties referenced above, we also lease a number of small sales and marketing offices in the United States and internationally. As of September 30, 2012, we were productively utilizing substantially all of the space in our facilities, except for space that has been subleased to third parties.

Item 3. Legal Proceedings

Like many companies in the software industry, we have from time to time been notified of claims that we may be infringing certain intellectual property rights of others. These claims have been referred to counsel, and they are in various stages of evaluation and negotiation. If it appears necessary or desirable, we may seek licenses for these intellectual property rights. There is no assurance that licenses will be offered by all claimants, that the terms of any offered licenses will be acceptable to us or that in all cases the dispute will be resolved without litigation, which may be time consuming and expensive, and may result in injunctive relief or the payment of damages by us. We do not consider the matters to be material either individually or in the aggregate at this time. Our view of the matters may change in the future as events related thereto unfold.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II

Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

Our common stock is traded on the NASDAQ Global Select Market under the symbol "NUAN". The following table sets forth, for our fiscal quarters indicated, the high and low sales prices of our common stock, in each case as reported on the NASDAQ Global Select Market.

	Low	High
Fiscal 2011:		
First quarter	\$ 14.79	\$ 19.19
Second quarter	16.79	20.97
Third quarter	18.85	22.93
Fourth quarter	15.56	22.40
Fiscal 2012:		
First quarter	\$ 19.28	\$ 26.97
Second quarter	24.37	31.15
Third quarter	19.33	26.85
Fourth quarter	19.58	25.89

Holders

As of October 31, 2012, there were 765 stockholders of record of our common stock.

Dividend Policy

We have never declared or paid any cash dividends on our common stock. We currently expect to retain future earnings, if any, to finance the growth and development of our business and do not anticipate paying any cash dividends in the foreseeable future. Furthermore, the terms of our credit facility place restrictions on our ability to pay dividends, except for stock dividends.

Issuer Purchases of Equity Securities

We have not announced any currently effective authorization to repurchase shares of our common stock.

Unregistered Sales of Equity Securities and Use of Proceeds

On August 14, 2012, we issued 795,848 shares of our common stock to International Business Machines Corporation as consideration for a collaboration agreement. The shares were issued in reliance upon an exemption from the registration requirements of the Securities Act of 1933, as amended, provided by Section 4(2) thereof because the issuance did not involve a public offering.

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Item 6. Selected Consolidated Financial Data

The following selected consolidated financial data is not necessarily indicative of the results of future operations and should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K (as adjusted for the retrospective application of FASB ASC 470-20 in 2009 and 2008).

	Fiscal Year Ended September 30,					
	2012	2011	2010	2009	2008	
Operations:						
Total revenues	\$1,651.5	\$1,318.7	\$1,118.9	\$950.4	\$868.5	
Gross profit	1,046.6	818.9	709.6	590.8	552.8	
Income from operations	126.2	52.6	32.9	57.6	32.6	
(Benefit) provision for income taxes	(141.8)	(8.2)	18.0	40.4	14.6	
Net income (loss)	\$207.1	\$38.2	\$(19.1)	\$(19.4)	\$(37.0)	
Net Income(Loss) Per Share Data:						
Basic	\$0.67	\$0.13	\$(0.07)	\$(0.08)	\$(0.18)	
Diluted	\$0.65	\$0.12	\$(0.07)	\$(0.08)	\$(0.18)	
Weighted average common shares outstanding:						
Basic	306.4	302.3	287.4	253.6	209.8	
Diluted	320.8	316.0	287.4	253.6	209.8	
Financial Position:						
Cash and cash equivalents and marketable securities	\$1,129.8	\$478.5	\$550.0	\$527.0	\$261.6	
Total assets	5,799.0	4,095.3	3,769.7	3,499.5	2,846.0	
Long-term debt, net of current portion	1,735.8	853.0	851.0	848.9	847.3	
Total stockholders’ equity	2,728.3	2,493.4	2,297.2	2,043.0	1,471.7	
Selected Data and Ratios:						
Working capital	\$736.5	\$379.9	\$459.2	\$376.6	\$133.5	
Depreciation of property and equipment	31.7	27.6	21.6	18.7	16.4	
Amortization of intangible assets	155.5	143.3	135.6	115.4	82.6	
Gross margin percentage	63.4	% 62.1	% 63.4	% 62.2	% 63.7	%

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following Management’s Discussion and Analysis is intended to help the reader understand the results of operations and financial condition of our business. Management’s Discussion and Analysis is provided as a supplement to, and should be read in conjunction with, our consolidated financial statements and the accompanying notes to the consolidated financial statements.

Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve risks, uncertainties and assumptions that, if they never materialize or if they prove incorrect, could cause our consolidated results to differ materially from those expressed or implied by such forward-looking statements. These forward-looking statements include predictions regarding:

- our future revenue, cost of revenue, research and development expenses, selling, general and administrative expenses, amortization of intangible assets and gross margin;
- our strategy relating to our segments;

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the potential of future product releases;
our product development plans and investments in research and development;
future acquisitions, and anticipated benefits from acquisitions;
international operations and localized versions of our products; and
legal proceedings and litigation matters.

You can identify these and other forward-looking statements by the use of words such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “intends,” “potential,” “continue” or the negative of such terms, or other comparable terminology. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks described in Item 1A — “Risk Factors” and elsewhere in this Annual Report on Form 10-K.

You should not place undue reliance on these forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K. We undertake no obligation to publicly release any revisions to the forward-looking statements or reflect events or circumstances after the date of this document.

Overview

We are a leading provider of voice and language solutions for businesses and consumers around the world. Our solutions are used in healthcare, mobile, consumer, enterprise customer service, and imaging markets. We offer market-leading accuracy, natural language understanding capability, domain knowledge and implementation capabilities, built on our significant, long-term investments in research and development. Our solutions are based on our proprietary voice and language platform and are used every day by millions of people and thousands of businesses for tasks and services such as requesting information from a phone-based self-service solution, dictating medical records, searching the mobile Web by voice, entering a destination into a navigation system, or working with PDF documents. We offer our solutions to our customers in a variety of ways, including through products, hosting, professional services and maintenance and support. Our product revenues include embedded OEM royalties, traditional enterprise licensing, term-based enterprise licensing and consumer-based sales. Our hosting revenues are primarily generated through on-demand service models, comprised of hosted transaction-based pricing arrangements that typically have multi-year terms. Our hosting and maintenance and support revenues are recurring in nature as our customers need to use our products on a repeat basis to handle their needs in medical transcription, enterprise customer service and mobile connected services. Our professional services also offer a visible revenue stream, as we have a backlog of assignments that take time to complete.

We are organized in four segments; Healthcare, Mobile and Consumer, Enterprise, and Imaging. Our solutions and services address our four segments:

Healthcare. We provide a comprehensive set of solutions and services that support the clinical documentation process from capturing the patient encounter with their physician, to improved clinical documentation, coding, compliance and reimbursement. Our hosted and on-premise solutions provide platforms to generate and distribute clinical documentation through the use of advanced dictation and transcription features, and allow us to deliver scalable, highly productive medical transcription solutions. We offer solutions that leverage the captured information and with state-of-the-art coding, compliance and record management which streamlines health information management ("HIM") processes to drive compliance and reimbursement. Through Clinical Documentation Improvement programs, we bridge the gap between physicians and coders. These solutions will significantly streamline speed and completeness of documentation so that providers can shorten the time between the patient visit and the payment for that visit. Our solutions also enable us to accelerate future innovation to transform the way healthcare providers

document patient care, through improved interface with electronic medical records and extraction of clinical information to support the billing and insurance reimbursement processes. We also offer speech recognition solutions for radiology, cardiology, pathology and related specialties, that help healthcare providers dictate, edit and sign reports without manual transcription. Trends in our healthcare business include a growing customer preference for hosted solutions, increasing interest in the use of mobile devices to access healthcare systems and records, and increasing international interest. We continue to see strong demand for transactions which involve the sale and delivery of both software and non-software related services or products. Over the last several quarters, we have signed several new contracts for our hosted solutions, and the volume of lines processed in these services has steadily increased. We are investing to expand our product set to address these opportunities, expand our international capabilities, and reduce our time from contract signing to initiation of billable services.

Mobile and Consumer. Our portfolio of mobile and consumer solutions and services includes an integrated suite of

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voice control and text-to-speech solutions, dictation applications, predictive text technologies, mobile messaging services and emerging services such as dictation, Web search and voicemail-to-text. Our suite of Dragon general purpose desktop and portable computer dictation applications increases productivity by using speech to create documents, streamline repetitive and complex tasks, input data, complete forms and automate manual transcription processes. In particular, we have focused in recent quarters on integrating our Dragon technology and brand initiatives across mobile and consumer markets. Trends in our mobile-consumer segment include device manufacturers requiring custom applications to deliver unique and differentiated products, broadening keyboard technologies to take advantage of touch screens, increasing hands-free capabilities on cell phones and automobiles to address the growing concern of distracted driving, and the adoption of our technology on a broadening scope of devices, such as televisions, set-top boxes, e-book readers and tablet computers. We continue to see strong demand for transactions which involve the sale and delivery of both software and non-software related services or products. We are investing to increase our capabilities and capacity to help device manufacturers build custom applications, to increase the capacity of our data centers, to increase the number, kinds and capacity of network services, to enable developers to access our technology, and to expand both awareness and channels for our direct-to-consumer products.

Enterprise. We deliver a portfolio of customer service business intelligence and authentication solutions that are designed to help companies better support, understand and communicate with their customers. Our solutions include the use of technologies such as speech recognition, natural language understanding, text-to-speech, biometric voice recognition and analytics to automate caller identification and authorization, call steering, completion of tasks such as updates, purchases and information retrieval, and automated outbound notifications. Our solutions improve the customer experience, increase the use of self-service and enable new revenue opportunities. In addition, we offer solutions that can meet customer care needs through

- direct interaction with thin-client applications on cell phones, enabling customers to very quickly retrieve relevant information. Trends in our enterprise business include increasing interest in the use of mobile applications to access customer care systems and records, increasing interest in coordinating actions and data across customer care channels, and the ability of a broader set of hardware providers and systems integrators to serve the market. We are investing to expand our product set to address these opportunities, to increase efficiency of our hosted applications, expand our capabilities and capacity to help customers build custom applications, and broaden our relationships with new hardware and systems integrator partners serving the market.

Imaging. Our imaging solutions offer optical character recognition technology to deliver highly accurate document scanning and storage. We provide networked print management and comprehensive PDF applications designed specifically for business users. In addition, we offer applications that combine network scanning, network print management and PDF creation to quickly enable distribution of documents to users' desktops or to enterprise applications. Our host of services includes software development toolkits for independent software vendors. The imaging market is evolving to include more networked solutions, mobile access to networked solutions, and multi-function devices. We are investing to improve mobile access to our networked products, expand our distribution channels and embedding relationships, and expand our language coverage.

We leverage our global professional services organization and our extensive network of partners to design and deploy innovative solutions for businesses and organizations around the globe. We market and sell our products directly through a dedicated sales force and through our e-commerce website and also through a global network of resellers, including system integrators, independent software vendors, value-added resellers, hardware vendors, telecommunications carriers and distributors.

We have built a world-class portfolio of intellectual property, technologies, applications and solutions through both internal development and acquisitions. We expect to continue to pursue opportunities to broaden these assets and expand our customer base through acquisitions.

Confronted by dramatic increases in electronic information, consumers, business personnel and healthcare professionals must use a variety of resources to retrieve information, transcribe patient records, conduct transactions and perform other job-related functions. We believe that the power of our solutions can transform the way people use the Internet, telecommunications systems, electronic medical records, wireless and mobile networks and related corporate infrastructure to conduct business.

Strategy

In fiscal 2013, we will continue to focus on growth by providing market-leading, value-added solutions for our customers and partners through a broad set of technologies, service offerings and channel capabilities. We will also continue to focus on operating efficiencies, expense discipline and acquisition synergies to improve gross margins and operating margins. We intend to pursue growth through the following key elements of our strategy:

Extend Technology Leadership. Our solutions are recognized as among the best in their respective categories. We intend

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to leverage our global research and development organization and broad portfolio of technologies, applications and intellectual property to foster technological innovation and maintain customer preference for our solutions. We also intend to invest in our engineering resources and seek new technological advancements that further expand the addressable markets for our solutions.

Broaden Expertise in Vertical Markets. Businesses are increasingly turning to Nuance for comprehensive solutions rather than for a single technology product. We intend to broaden our expertise and capabilities to deliver targeted solutions for a range of industries including mobile device manufacturers, healthcare, telecommunications, financial services and government administration. We also intend to expand our global sales and professional services capabilities to help our customers and partners design, integrate and deploy innovative solutions.

Increase Subscription and Transaction Based Recurring Revenue. We intend to increase our subscription and transaction based offerings in our segments. The expansion of our subscription or transaction based solutions will enable us to deliver applications that our customers use on a repeat basis, and pay for on a per use basis, providing us with the opportunity to enjoy the benefits of recurring revenue streams.

Expand Global Presence. We intend to further expand our international resources to better serve our global customers and partners and to leverage opportunities in emerging markets such as Asia and Latin America. We continue to add regional executives and sales employees in different geographic regions to better address demand for voice and language based solutions and services.

Pursue Strategic Acquisitions and Partnerships. We have selectively pursued strategic acquisitions to expand our technology, solutions and resources to complement our organic growth. We have also formed key partnerships with other important companies in our markets of interest, and intend to continue to do so in the future where it will enhance the value of our business. We have proven experience in integrating businesses and technologies and in delivering enhanced value to our customers, partners, employees and shareholders. We intend to continue to pursue acquisitions that enhance our solutions, serve specific vertical markets and strengthen our technology portfolio.

Key Metrics

In evaluating the financial condition and operating performance of our business, management focuses on revenue, net income, gross margins, operating margins and cash flow from operations. A summary of these key financial metrics for the fiscal year ended September 30, 2012, as compared to the fiscal year ended September 30, 2011, is as follows:

- Total revenue increased by \$332.8 million to \$1,651.5 million;
- Net income improved by \$168.9 million to \$207.1 million;
- Gross margins increased by 1.3 percentage points to 63.4%;
- Operating margins increased by 3.6 percentage point to 7.6%; and
- Cash provided by operating activities for the fiscal year ended September 30, 2012 was \$473.0 million, an increase of \$115.6 million from the prior fiscal year.

In addition to the above key financial metrics, we also focus on certain non-financial performance indicators. A summary of these key non-financial performance indicators as of and for the period ended September 30, 2012, as compared to September 30, 2011, is as follows:

• Annualized line run-rate in our on-demand healthcare solutions increased 21% to approximately 4.8 billion lines per year. The annualized line run-rate is determined using billed equivalent line counts in a given quarter, multiplied by four; and

• Estimated 3-year value of on-demand contracts increased 43% to approximately \$1.9 billion. We determine this value by using our best estimate of all anticipated future revenue streams under signed on-demand contracts currently in place, whether or not they are guaranteed through a minimum commitment clause. Our best estimate is based on assumptions about launch dates, volumes and renewal rates within the three year period. Most of these contracts are priced by volume of usage and typically have no or low minimum commitments. Actual revenue could vary from our

estimates due to factors such as cancellations, non-renewals or volume fluctuations.

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RESULTS OF OPERATIONS

Total Revenues

The following tables show total revenues by product type and revenue by geographic location, based on the location of our customers, in dollars and percentage change (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Product and licensing	\$740.7	\$607.4	\$473.5	21.9	% 28.3	%
Professional services and hosting	674.0	509.1	463.5	32.4	% 9.8	%
Maintenance and support	236.8	202.2	181.9	17.1	% 11.2	%
Total Revenues	\$1,651.5	\$1,318.7	\$1,118.9	25.2	% 17.9	%
United States	\$1,175.2	\$963.7	\$802.0	21.9	% 20.2	%
International	476.3	355.0	316.9	34.2	% 12.0	%
Total Revenues	\$1,651.5	\$1,318.7	\$1,118.9	25.2	% 17.9	%

Fiscal 2012 Compared to Fiscal 2011

The geographic split for fiscal 2012 was 71% of total revenue in the United States and 29% internationally, as compared to 73% of total revenue in the United States and 27% internationally for the same period last year. The increase in the proportion of revenue generated internationally was primarily due to contributions from our Mobile and Consumer and Imaging segments.

Fiscal 2011 Compared to Fiscal 2010

The geographic split for fiscal 2011 was 73% of total revenue in the United States and 27% internationally, as compared to 72% of total revenue in the United States and 28% internationally for the same period last year. The increase in the proportion of revenue generated domestically was primarily due to contributions from our Healthcare on-demand solutions, which are sold predominantly in the United States.

Product and Licensing Revenue

Product and licensing revenue primarily consists of sales and licenses of our technology. The following table shows product and licensing revenue, in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Product and licensing revenue	\$740.7	\$607.4	\$473.5	21.9	% 28.3	%
As a percentage of total revenues	44.9	% 46.1	% 42.3	%		

Fiscal 2012 Compared to Fiscal 2011

Product and licensing revenue for fiscal 2012 increased \$133.3 million, as compared to fiscal 2011. The increase consisted of a \$74.6 million increase in Mobile and Consumer revenue primarily driven by growth in sales of our embedded solutions. Imaging product and licensing revenue increased \$36.1 million, primarily driven by sales of our multi-functional peripheral (“MFP”) products, which included revenue associated with our acquisition of Equitrac in the third quarter of fiscal 2011.

Fiscal 2011 Compared to Fiscal 2010

Product and licensing revenue for fiscal 2011 increased \$133.9 million, as compared to fiscal 2010. The increase consisted of a \$50.1 million increase in Mobile and Consumer revenue primarily driven by \$31.6 million of growth in sales of our embedded solutions, and additional sales of \$18.5 million of Dragon consumer products. Imaging revenue increased by \$43.9 million, due to increased revenue from our MFP products. Healthcare revenue increased by \$23.0 million resulting in part from continued strength in Dragon Medical solutions, which represented \$12.8 million of the increase during the year. Enterprise on-premise license sales increased by \$16.9 million resulting from the continued increase in global demand for our core speech solutions.

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Professional Services and Hosting Revenue

Professional services revenue primarily consists of consulting, implementation and training services for customers. Hosting revenue primarily relates to delivering hosted services, such as medical transcription, automated customer care applications, voice message transcription, and mobile search and transcription, over a specified term. The following table shows professional services and hosting revenue, in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010
Professional services and hosting revenue	\$674.0	\$509.1	\$463.5	32.4	% 9.8
As a percentage of total revenues	40.8	% 38.6	% 41.4	%	%

Fiscal 2012 Compared to Fiscal 2011

Professional services and hosting revenue for fiscal 2012 increased \$164.9 million, as compared to fiscal 2011. The increase consisted of a \$130.6 million increase in Healthcare revenue primarily driven by transactional volume growth in our on-demand solutions, of which \$77.4 million was due to our acquisitions closed during fiscal 2011 and 2012. Mobile and Consumer revenue increased \$30.9 million, primarily attributable to a \$16.0 million increase in professional services to support the implementation of our embedded handset and automotive solutions and a \$13.4 million increase driven by transactional volume growth in our connected mobile services.

Fiscal 2011 Compared to Fiscal 2010

Professional services and hosting revenue for fiscal 2011 increased \$45.6 million, as compared to fiscal 2010. The increase consisted of a \$40.1 million increase in Healthcare revenue primarily driven by transactional volume growth in our on-demand solutions. Mobile and Consumer revenue increased \$29.3 million as a result of growth of \$19.2 million in our connected mobile services and growth of \$10.1 million in professional services for our embedded solutions. Enterprise revenue decreased by \$24.4 million, primarily due to the decline of one on-demand customer's volume.

Maintenance and Support Revenue

Maintenance and support revenue primarily consists of technical support and maintenance services. The following table shows maintenance and support revenue, in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010
Maintenance and support revenue	\$236.8	\$202.2	\$181.9	17.1	% 11.2
As a percentage of total revenues	14.3	% 15.3	% 16.3	%	%

Fiscal 2012 Compared to Fiscal 2011

Maintenance and support revenue for fiscal 2012 increased \$34.6 million, as compared to fiscal 2011. The increase was driven by growth in our product and licensing sales which included a \$15.8 million increase in Imaging revenue primarily due to our acquisition of Equitrac, and a \$10.2 million increase in Healthcare revenue driven by growth in sales of our Dragon Medical solutions.

Fiscal 2011 Compared to Fiscal 2010

Maintenance and support revenue for fiscal 2011 increased \$20.3 million, as compared to fiscal 2010. The increase was driven by growth in our product and licensing sales which included a \$7.5 million increase in Healthcare driven by Dragon Medical solutions, a \$5.5 million increase in Enterprise, and a \$5.3 million increase in Imaging with contributions from our acquisition of Equitrac.

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COSTS AND EXPENSES

Cost of Product and Licensing Revenue

Cost of product and licensing revenue primarily consists of material and fulfillment costs, manufacturing and operations costs and third-party royalty expenses. The following table shows cost of product and licensing revenue, in dollars and as a percentage of product and licensing revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Cost of product and licensing revenue	\$74.8	\$65.6	\$49.6	14.0	% 32.3	%
As a percentage of product and licensing revenue	10.1	% 10.8	% 10.5	%		

Fiscal 2012 Compared to Fiscal 2011

Cost of product and licensing revenue for fiscal 2012 increased \$9.2 million, as compared to fiscal 2011. The increase was primarily due to a \$5.0 million increase in Imaging costs driven by our acquisition of Equitrac. Gross margin increased 0.7 percentage points primarily due to a mix shift toward our Mobile embedded solutions which carry a higher gross margin.

Fiscal 2011 Compared to Fiscal 2010

Cost of product and licensing revenue for fiscal 2011 increased \$16.0 million, as compared to fiscal 2010. The increase was primarily due to an increase in hardware costs associated with increased revenues from our MFP products in the Imaging segment. Gross margin remained relatively flat during the period.

Cost of Professional Services and Hosting Revenue

Cost of professional services and hosting revenue primarily consists of compensation for services personnel, outside consultants and overhead, as well as the hardware, infrastructure and communications fees that support our hosting solutions. The following table shows cost of professional services and hosting revenue, in dollars and as a percentage of professional services and hosting revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Cost of professional services and hosting revenue	\$424.7	\$341.1	\$280.7	24.5	% 21.5	%
As a percentage of professional services and hosting revenue	63.0	% 67.0	% 60.6	%		

Fiscal 2012 Compared to Fiscal 2011

Cost of professional services and hosting revenue for fiscal 2012 increased \$83.6 million, as compared to fiscal 2011. The increase was primarily driven by a \$73.5 million increase in Healthcare costs related to growth in our on-demand solutions, including the impact from our acquisitions closed during fiscal 2011 and 2012. Gross margin increased 4.0 percentage points primarily due to a mix shift toward our Healthcare on-demand offerings which carry a higher gross margin and expanded margins due to an increase in automation services relating to our connected mobile solutions in our Mobile and Consumer segment.

Fiscal 2011 Compared to Fiscal 2010

Cost of professional services and hosting revenue for fiscal 2011 increased \$60.4 million, as compared to fiscal 2010. The increase was due to a \$29.6 million increase in Healthcare costs primarily related to growth in our on-demand solutions, and a \$16.8 million increase in stock-based compensation related to our professional services personnel. Gross margin relative to our professional services and hosting revenue decreased 6.4 percentage points primarily due to increased stock-based compensation expense reducing gross margin by 3.3 percentage points and the remainder is primarily related to volume and revenue declines from one on-demand Enterprise customer.

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Cost of Maintenance and Support Revenue

Cost of maintenance and support revenue primarily consists of compensation for product support personnel and overhead. The following table shows cost of maintenance and support revenue, in dollars and as a percentage of maintenance and support revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Cost of maintenance and support revenue	\$45.3	\$38.1	\$31.3	18.9	% 21.7	%
As a percentage of maintenance and support revenue	19.1	% 18.8	% 17.2	%		

Fiscal 2012 Compared to Fiscal 2011

Cost of maintenance and support revenue for fiscal 2012 increased \$7.2 million, as compared to fiscal 2011. The increase was primarily due to a \$6.9 million increase in Imaging costs related to the increase revenues from our Imaging MFP products, which included the impact from the Equitrac acquisition in fiscal 2011. Gross margin remained relatively flat during the period.

Fiscal 2011 Compared to Fiscal 2010

Cost of maintenance and support revenue for fiscal 2011 increased \$6.8 million, as compared to fiscal 2010. The increase included a \$2.5 million increase in costs due to higher volumes of Enterprise application maintenance and support, a \$2.1 million increase in costs related to increased revenue from our MFP products in our Imaging business, which included the impact from our acquisition of Equitrac, and a \$1.4 million increase in stock-based compensation expense. The increase in stock-based compensation expense reduced gross margin by 0.7% during the period. Excluding impact from stock-based compensation, gross margin remained relatively flat during the period.

Research and Development Expense

Research and development expense primarily consists of salaries, benefits and overhead relating to engineering staff as well as third party engineering costs. The following table shows research and development expense, in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Research and development expense	\$225.4	\$179.4	\$152.1	25.6	% 17.9	%
As a percentage of total revenues	13.6	% 13.6	% 13.6	%		

Fiscal 2012 Compared to Fiscal 2011

Research and development expense for fiscal 2012 increased \$46.0 million, as compared to fiscal 2011. The increase was attributable to a \$35.8 million increase in compensation expense, driven by headcount growth including additional headcount from our acquisitions during the period.

Fiscal 2011 Compared to Fiscal 2010

Research and development expense for fiscal 2011 increased \$27.3 million, as compared to fiscal 2010. The increase was attributable to a \$28.6 million increase in compensation expense, driven by a \$14.9 million increase in stock-based compensation expense and headcount growth as well as additional headcount from our acquisitions during the period. The increase was offset by reimbursement of \$5.9 million under a new collaboration agreement signed during the period as discussed in Note 2 of our Notes to Consolidated Financial Statements.

Sales and Marketing Expense

Sales and marketing expense includes salaries and benefits, commissions, advertising, direct mail, public relations, tradeshow costs and other costs of marketing programs, travel expenses associated with our sales organization and overhead. The following

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table shows sales and marketing expense, in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010
Sales and marketing expense	\$369.2	\$306.4	\$266.2	20.5	% 15.1
As a percentage of total revenues	22.4	% 23.2	% 23.8	%	

Fiscal 2012 Compared to Fiscal 2011

Sales and marketing expense for fiscal 2012 increased \$62.8 million, as compared to fiscal 2011. The increase was primarily attributable to a \$35.9 million increase in compensation expense, driven primarily by additional headcount due to operational and acquisition growth and increased stock-based compensation expense. Additionally, marketing and channel program spending increased \$18.6 million to drive revenue growth as part of demand generation activities.

Fiscal 2011 Compared to Fiscal 2010

Sales and marketing expense for fiscal 2011 increased \$40.2 million, as compared to fiscal 2010. The increase was primarily attributable to a \$21.7 million increase in compensation expense, driven primarily by additional headcount to support growth and a \$5.1 million increase in stock-based compensation expense. Additionally, marketing and channel program spending increased \$14.0 million to drive overall revenue growth.

General and Administrative Expense

General and administrative expense primarily consists of personnel costs for administration, finance, human resources, information systems, facilities and general management, fees for external professional advisers including accountants and attorneys, insurance, and provisions for doubtful accounts. The following table shows general and administrative expense, in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010
General and administrative expense	\$163.3	\$147.6	\$122.1	10.6	% 20.9
As a percentage of total revenues	9.9	% 11.2	% 10.9	%	

Fiscal 2012 Compared to Fiscal 2011

General and administrative expense for fiscal 2012 increased \$15.7 million, as compared to fiscal 2011. The increase was primarily attributable to a \$26.8 million increase in compensation expense, driven primarily by additional headcount due to organic and acquisition growth and increased stock-based compensation expense, offset by a \$11.0 million decrease in legal costs primarily associated with decrease in on-going litigation activities.

Fiscal 2011 Compared to Fiscal 2010

General and administrative expense for fiscal 2011 increased \$25.5 million, as compared to fiscal 2010. The increase was primarily attributable to a \$14.5 million increase in compensation expense and a \$9.1 million increase in legal costs associated with on-going litigation and intellectual property maintenance. The increase in compensation expense was driven primarily by additional headcount due to organic growth and our acquisitions during the period and an \$8.9 million increase in stock-based compensation expense.

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Amortization of Intangible Assets

Amortization of acquired patents and core and completed technology are included in cost of revenue and the amortization of acquired customer and contractual relationships, non-compete agreements, acquired trade names and trademarks, and other intangibles are included in operating expenses. Customer relationships are amortized on an accelerated basis based upon the pattern in which the economic benefits of the customer relationships are being realized. Other identifiable intangible assets are amortized on a straight-line basis over their estimated useful lives. Amortization expense was recorded as follows (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Cost of revenue	\$60.0	\$55.1	\$47.8	8.9	% 15.3	%
Operating expense	95.4	88.2	87.8	8.2	% 0.5	%
Total amortization expense	\$155.4	\$143.3	\$135.6	8.4	% 5.7	%
As a percentage of total revenues	9.4	% 10.9	% 12.1	%		

Fiscal 2012 Compared to Fiscal 2011

Amortization of intangible assets expense for fiscal 2012 increased \$12.1 million, as compared to fiscal 2011. The increase was primarily attributable to the amortization of acquired customer relationships from our business acquisitions during fiscal 2012 and the second half of fiscal 2011.

Fiscal 2011 Compared to Fiscal 2010

Amortization of intangible assets expense for fiscal 2011 increased \$7.7 million, as compared to fiscal 2010. The increase was primarily attributable to the amortization of acquired technology and patent intangible assets from our business acquisitions during fiscal 2011 and our acquisitions of patents and technology from third-parties during the fiscal 2010.

Based on our balance of amortizable intangible assets as of September 30, 2012, and assuming no impairment or change in useful lives, we expect amortization of intangible assets for fiscal 2013 to be \$150.6 million.

Acquisition-Related Costs, Net

Acquisition-related costs include those costs related to business and other acquisitions, including potential acquisitions. These costs consist of (i) transition and integration costs, including retention payments, transitional employee costs and earn-out payments treated as compensation expense, as well as the costs of integration-related services provided by third-parties; (ii) professional service fees, including third-party costs related to the acquisition, and legal and other professional service fees associated with disputes and regulatory matters related to acquired entities; and (iii) adjustments to acquisition-related items that are required to be marked to fair value each reporting period, such as contingent consideration, and other items related to acquisitions for which the measurement period has ended. Acquisition-related costs were recorded as follows (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Professional service fees	\$48.4	\$18.0	\$17.1	168.9	% 5.3	%
Transition and integration costs	9.9	3.4	13.6	191.2	% (75.0))%
Acquisition-related adjustments	0.4	0.5	(0.1	) (20.0	)% (600.0))%
	\$58.7	\$21.9	\$30.6	168.0	% (28.4))%

Total Acquisition-related costs,
net

As a percentage of total revenue 3.6 % 1.7 % 2.7 %

Fiscal 2012 Compared to Fiscal 2011

Acquisition-related costs, net for fiscal 2012 increased \$36.8 million, as compared to fiscal 2011. The increase was primarily driven by an increase in professional fees incurred associated with the post-acquisition legal and regulatory costs associated with recently completed acquisitions. For fiscal 2012, transition and integration costs consisted primarily of the costs associated with transitional employees from our acquisition of Swype.

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Fiscal 2011 Compared to Fiscal 2010

Acquisition-related costs, net for fiscal 2011 decreased \$8.7 million, as compared to fiscal 2010. The decrease was primarily driven by the reduction in transition and integration costs. For fiscal 2010, \$8.9 million of transition and integration costs was driven by our acquisitions of eCopy and SpinVox.

Restructuring and Other Charges, Net

The following table sets forth the activity relating to the restructuring accruals included in Restructuring and Other Charges, net, in fiscal 2012, 2011 and 2010 (dollars in millions):

	Personnel Related	Facilities Costs	Other	Total
Balance at September 30, 2009	0.6	0.3	—	0.9
Restructuring and other charges, net	9.6	0.2	8.9	18.7
Non-cash adjustments	—	—	(6.8)	(6.8)
Cash payments	(8.4)	(0.2)	(2.1)	(10.7)
Balance at September 30, 2010	1.8	0.3	—	2.1
Restructuring and other charges, net	9.1	1.9	12.0	23.0
Non-cash adjustments	0.2	—	(11.9)	(11.7)
Cash payments	(6.0)	(1.2)	(0.1)	(7.3)
Balance at September 30, 2011	5.1	1.0	—	6.1
Restructuring and other charges, net	6.7	0.4	0.4	7.5
Cash payments	(10.1)	(1.3)	(0.4)	(11.8)
Balance at September 30, 2012	\$1.7	\$0.1	\$—	\$1.8

For fiscal 2012, we recorded net restructuring and other charges of \$7.5 million, which included a \$6.7 million severance charge related to the elimination of approximately 160 personnel across multiple functions primarily to eliminate duplicative positions as a result of businesses acquired.

For fiscal 2011, we recorded net restructuring and other charges of \$23.0 million, which consisted primarily of an \$11.7 million impairment charge related to our Dictaphone trade name resulting from a recent change in our Healthcare marketing strategy under which we plan to consolidate our brands and will no longer be using the Dictaphone trade name in our new product offerings. In addition, we recorded a \$9.1 million charge related to the elimination of approximately 200 personnel across multiple functions primarily to eliminate duplicative positions as a result of businesses acquired during the year and a \$1.9 million charge related to the elimination or consolidation of excess facilities.

For fiscal 2010, we recorded net restructuring and other charges of \$18.7 million, which consisted primarily of \$9.6 million related to the elimination of approximately 175 personnel across multiple functions within our company, including acquired entities, a \$6.8 million write-off of previously capitalized patent defense costs as a result of unsuccessful litigation and \$2.1 million of contract termination costs.

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Other Income (Expense)

Other income (expense) consists of interest income, interest expense, gain (loss) from security price guarantee derivatives, gain (loss) from foreign exchange, and gains (losses) from other non-operating activities. The following table shows other income (expense) in dollars and as a percentage of total revenue (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010
Interest income	\$2.2	\$3.2	\$1.2	(31.3)	)% 166.7
Interest expense	(85.3)	) (36.7)	) (41.0)	132.4	% (10.5)
Other income, net	22.2	11.0	5.8	101.8	% 89.7
Total other expense, net	\$(60.9)	) \$(22.5)	) \$(34.0)		
As a percentage of total revenue	3.7	% 1.7	% 3.0	%	

Fiscal 2012 Compared to Fiscal 2011

Interest expense for fiscal 2012 increased \$48.6 million, as compared to fiscal 2011. The increase in interest expense was due to the issuance of \$690 million of 2.75% Convertible Debentures due in 2031 in the first quarter of fiscal 2012 and \$700 million of 5.375% Senior Notes due in 2020 in the fourth quarter of fiscal 2012. This increased cash interest expense by \$22.7 million and non-cash interest by \$21.8 million.

Other income, net for fiscal 2012 increased \$11.2 million, as compared to fiscal 2011. The increase was primarily driven by a \$13.7 million gain recognized on the original non-controlling equity interest in Vlingo upon our acquisition of Vlingo during the third quarter of fiscal 2012.

Fiscal 2011 Compared to Fiscal 2010

Interest expense for fiscal 2011 decreased \$4.3 million, as compared to fiscal 2010. The decrease in interest expense was primarily driven by decreased interest costs as a result of lower rates on our outstanding variable rate borrowings. Other income, net increased \$5.2 million, as compared to fiscal 2010, driven primarily by a \$9.3 million increase in gains on our security price guarantee derivatives. This was offset by a decrease in foreign exchange gains of \$4.7 million resulting from our implementation of a hedging program in fiscal 2011 to reduce our exposure to changes in foreign currency exchange rates.

(Benefit) Provision for Income Taxes

The following table shows the (benefit) provision for income taxes and the effective income tax rate (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010
(Benefit) provision for income taxes	\$(141.8)	) \$(8.2)	) \$18.0	1,629.3	% (145.6)
Effective income tax rate	(217.2)	)% (27.4)	)% (1,693.3))%	

Fiscal 2012 Compared to Fiscal 2011

Our effective income tax rate was (217.2)% and (27.4)% for fiscal 2012 and 2011, respectively. Benefit from income taxes increased \$133.6 million from \$8.2 million in fiscal 2011 to \$141.8 million in fiscal 2012. The increase in benefit from income taxes included the release of our valuation allowance resulting from our acquisitions during fiscal

2012 and the recognition of certain deferred tax assets. During fiscal 2012, we recorded a release of valuation allowance of \$75.1 million as a result of tax benefits recorded in connection with our acquisitions during the period for which a net deferred tax liability was established in purchase accounting. In addition, by the end of fiscal 2012, we made a determination that it is more likely than not that certain of our deferred tax assets, primarily in the U.S., will be realized which resulted in a release of \$70.5 million of our valuation allowance (See Note 20 of our Notes to Consolidated Financial Statements).

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Fiscal 2011 Compared to Fiscal 2010

Our effective income tax rate was (27.4)% and (1,693.3)% for fiscal 2011 and 2010, respectively. Provision for income taxes decreased \$26.2 million from a provision of \$18.0 million to a benefit of \$8.2 million. The decrease in the tax provision was primarily related to a tax benefit recorded in connection with the Equitrac acquisition for which a net deferred tax liability was recorded in purchase accounting, resulting in a release of our valuation allowance of \$34.7 million and therefore a tax benefit during the year. The decrease in the tax provision was also due to a release of \$10.6 million of our valuation allowance associated with the change in characterization of a previously acquired intangible asset from an indefinite life asset to a finite life asset during our fourth quarter of fiscal 2011. These deferred tax benefits were offset by a \$21.4 million increase in our current income tax provision primarily driven by higher U.S. taxable income.

SEGMENT ANALYSIS

We operate in, and report financial information for, the following four reportable segments: Healthcare, Mobile and Consumer, Enterprise and Imaging. The Healthcare segment is primarily engaged in voice and language processing for healthcare information management offered both by licensing and on-demand services. The Mobile and Consumer segment is primarily engaged in sales of voice and language solutions that are embedded in a device (such as a cell phone, car or tablet computer) or installed on a personal computer. Our Enterprise segment offers voice and language solutions by licensing as well as on-demand solutions hosted by us that are designed to help companies better support, understand and communicate with their customers. The Imaging segment sells document capture and print management solutions that are embedded in copiers and multi-function printers as well as packaged software for document management.

Segment revenues include certain revenue adjustments related to acquisitions that would otherwise have been recognized but for the purchase accounting treatment of the business combinations. Segment revenues also include revenue that we would have otherwise recognized had we not acquired intellectual property and other assets from the same customer during the same quarter. We include these revenues and the related cost of revenues to allow for more complete comparisons to the financial results of historical operations, forward-looking guidance and the financial results of peer companies and in assessing management performance.

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Segment profit is an important measure used for evaluating performance and for decision-making purposes. Segment profit reflects the direct controllable costs of each segment together with an allocation of sales and corporate marketing expenses, and certain research and development project costs that benefit multiple product offerings. Segment profit represents income from operations excluding stock-based compensation, amortization of intangible assets, acquisition-related costs, net, restructuring and other charges, net, costs associated with intellectual property collaboration agreements, other income (expense), net and certain unallocated corporate expenses. Segment profit includes an adjustment for acquisition-related revenues and cost of revenues which includes revenue from acquisitions that would have otherwise been recognized but for the purchase accounting treatment of these transactions. We believe that these adjustments allow for more complete comparisons to the financial results of the historical operations. The following table presents segment results (dollars in millions):

	Fiscal 2012	Fiscal 2011	Fiscal 2010	% Change 2012 vs. 2011	% Change 2011 vs. 2010	
Segment Revenues						
Healthcare	\$669.4	\$526.8	\$449.2	27.1	% 17.3	%
Mobile and Consumer	508.3	393.3	309.5	29.2	% 27.1	%
Enterprise	332.0	296.4	296.2	12.0	% 0.1	%
Imaging	228.4	177.4	140.7	28.7	% 26.1	%
Total segment revenues	\$1,738.1	\$1,393.9	\$1,195.6	24.7	% 16.6	%
Less: acquisition related revenues	(86.6)	(75.2)	(76.7)	15.2	% (2.0))%
Total revenues	\$1,651.5	\$1,318.7	\$1,118.9	25.2	% 17.9	%
Segment Profit						
Healthcare	\$314.9	\$269.4	\$227.4	16.9	% 18.5	%
Mobile and Consumer	227.6	170.9	120.0	33.2	% 42.4	%
Enterprise	90.8	63.3	82.3	43.4	% (23.1))%
Imaging	91.6	69.1	55.6	32.6	% 24.3	%
Total segment profit	\$724.9	\$572.7	\$485.3	26.6	% 18.0	%
Segment Profit Margin						
Healthcare	47.0	% 51.1	% 50.6	% (4.1)	0.5	
Mobile and Consumer	44.8	% 43.5	% 38.8	% 1.3	4.7	
Enterprise	27.3	% 21.4	% 27.8	% 5.9	(6.4)	
Imaging	40.1	% 39.0	% 39.5	% 1.1	(0.5)	
Total segment profit margin	41.7	% 41.1	% 40.6	% 0.6	0.5	

Segment Revenue

Fiscal 2012 Compared to Fiscal 2011

Healthcare segment revenue increased \$142.6 million, primarily attributable to revenue growth in on-demand solutions. Professional services and hosting revenue increased \$119.7 million due to growth in on-demand transactional volume, of which \$77.4 million of the increase was due to additional volume resulting from our acquisitions during fiscal 2011 and 2012.

Mobile and Consumer segment revenue increased \$115.0 million. Our product and licensing revenue grew \$83.3 million, mainly driven by growth in our embedded handset, automotive and other consumer electronics. Our professional services and hosting revenue grew \$32.8 million primarily driven by a \$17.7 million increase in professional services to support the implementations of our embedded handset and automotive solutions as well as a \$15.0 million increase driven by transactional volume growth in our connected mobile services.

Enterprise segment revenue increased \$35.6 million. Our product and licensing revenue grew \$25.0 million, driven primarily by contributions from our acquisition of Loquendo. Our maintenance and support revenue grew \$8.2 million from the continued strength in renewals.

Imaging segment revenue increased \$51.0 million. Our product and licensing revenue grew \$32.5 million and our maintenance and support grew \$18.2 million, primarily due to growth in sales from our MFP products driven by our acquisition of Equitrac.

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Fiscal 2011 Compared to Fiscal 2010

Healthcare segment revenue increased by \$77.6 million, primarily attributable to revenue growth in both licenses and on-demand solutions. On-demand revenue increased by \$47.2 million due to increased transactional volume. Product and licensing revenue increased by \$20.5 million due to volume and continued strong demand of our Healthcare license offerings resulting in part from continued strength in Dragon Medical solutions.

Mobile and Consumer segment revenue increased by \$83.8 million. Our product and licensing revenue grew \$57.4 million primarily related to growth of \$39.3 million in our embedded handset and automotive products and \$18.1 million in our Dragon products. Our professional services and hosting revenue grew \$24.5 million related to both the increased volume of transactions in our connected mobile services as well as professional services revenue to support the implementation of recent handset and automobile design wins.

Enterprise segment revenue remained flat from fiscal 2010 to fiscal 2011. Our product and licensing revenue grew \$18.8 million and maintenance and support revenue grew \$6.4 million resulting from the continued increase in global demand for our core speech solutions. These increases were offset by a decline of \$25.0 million in our professional services and hosting revenue, primarily attributable to the decline in volume from one on-demand customer.

Imaging segment revenue increased by \$36.7 million, primarily attributable to growth in sales from our MFP products, which includes the impact from our acquisition of Equitrac.

Segment Profit

Fiscal 2012 Compared to Fiscal 2011

Healthcare segment profit in fiscal 2012 increased \$45.5 million, or 16.9%, over fiscal 2011, driven primarily by segment revenue growth of 27.1%, partially offset by increased costs from growth in sales of our on-demand solutions. Segment profit margin decreased 4.1 percentage points from 51.1% in fiscal 2011 to 47.0% in fiscal 2012. This decrease was primarily driven by a decrease of 5.1 percentage points in margin due to a higher proportion of editing services in our on-demand offerings, which included impact of the Transcend acquisition, and a 0.6 percentage point improvement due to leveraging of selling expenses.

Mobile and Consumer segment profit in fiscal 2012 increased \$56.7 million, or 33.2%, over fiscal 2011, primarily due to segment revenue growth of 29.2%, partially offset by increased investment in research and development and marketing. Segment profit margin in fiscal 2012 improved 1.3 percentage points from 43.5% in fiscal 2011 to 44.8% in fiscal 2012. This increase was primarily driven by a 2.2 percentage point improvement in margin due to a favorable mix shift toward our embedded product revenue and a 2.5 percentage point improvement due to leveraging of selling expense. These improvements were offset by a 2.0 percentage point decrease in segment profit margin due to increased investment in research and development to support new product offerings and a 1.1 percentage point decrease as a result of higher marketing demand creation costs to drive Dragon consumer product sales.

Enterprise segment profit in fiscal 2012 increased \$27.5 million, or 43.4%, over fiscal 2011, driven primarily by segment revenue growth of 12.0%, partially offset by increased investment in sales expense. Segment profit margin in fiscal 2012 increased 5.9 percentage points from 21.4% in fiscal 2011 to 27.3% in fiscal 2012. This increase benefited from a favorable mix of product and licensing revenues which includes the impact of the acquisition of Loquendo, contributing to an increase in gross margins of 5.3 percentage points, as well as a 1.2 percentage point improvement driven by operating expense leverage in research and development.

Imaging segment profit in fiscal 2012 increased \$22.5 million, or 32.6%, over fiscal 2011, driven in part from a 28.7% increase in segment revenue, offset by increased investment in marketing and selling expenses. Segment profit margin increased 1.1 percentage points from 39.0% in fiscal 2011 to 40.1% in fiscal 2012. The change in segment profit margin included a 2.5 percentage point improvement due to leveraging selling expense, offset by 1.9 percentage points of segment margin erosion due to increased marketing spend to drive revenue growth.

Fiscal 2011 Compared to Fiscal 2010

Healthcare segment profit in fiscal 2011 increased \$42.0 million, or 18.5%, over fiscal 2010, driven primarily by segment revenue growth of 17.3%. Segment profit increased by 0.5 percentage points as a result of operating expense leverage and a \$5.9 million reimbursement under a new collaboration agreement signed during the period as discussed in Note 2 to the audited consolidated financial statements.

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Mobile and Consumer segment profit in fiscal 2011 increased \$50.9 million, or 42.4%, over fiscal 2010, resulting in part from the 27.1% increase in segment revenue. Segment profit margin in fiscal 2011 improved 4.7 percentage points from 38.8% in fiscal 2010 to 43.5% in fiscal 2011. The segment profit margin improvements were driven primarily by embedded and mobile services gross margin improvements, and from leverage in research and development and selling and marketing expenses.

Enterprise segment profit in fiscal 2011 decreased \$19.0 million, or 23.1%, over fiscal 2010, while sales were essentially flat. Segment profit margin in fiscal 2011 declined 6.4 percentage points from 27.8% in fiscal 2010 to 21.4% in fiscal 2011. This decrease was driven by decreased volume and revenue from one on-demand customer resulting in a 3.8 percentage point decrease in segment profit and increased spending in research and development contributed to a 1.7 percentage point decrease in segment profit.

Imaging segment profit in fiscal 2011 increased \$13.5 million, or 24.3%, over fiscal 2010, driven primarily by the 26.1% increase in sales. Segment profit margin in fiscal 2011 remained relatively flat at 39.0% in fiscal 2011 compared to 39.5% in fiscal 2010.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents totaled \$1,129.8 million as of September 30, 2012, an increase of \$682.6 million as compared to \$447.2 million as of September 30, 2011. Our working capital at September 30, 2012 was \$736.5 million compared to \$379.9 million of working capital at September 30, 2011. Cash and cash equivalents held by our international operations totaled \$78.8 million and \$61.7 million at September 30, 2012 and 2011, respectively. Based on our business plan, we expect the cash held overseas will continue to be used for our international operations and therefore do not anticipate repatriating these funds. If we were to repatriate these amounts, we do not believe that the resulting withholding taxes payable would have a material impact on our liquidity. As of September 30, 2012, our total accumulated deficit was \$161.2 million. We do not expect our accumulated deficit to impact our future ability to operate the business given our strong cash and operating cash flow positions.

On October 22, 2012, we issued \$350.0 million aggregate principal amount of our 5.375% Senior Notes due 2020 (the "Notes"). The Notes were issued pursuant to the indenture agreement dated August 14, 2012 related to our \$700.0 million aggregate principal amount of 5.375% Senior Notes due 2020 issued in the fourth quarter of fiscal 2012. Total proceeds, net of issuance costs, were \$353.3 million. On October 31, 2012, we used \$143.5 million of the net proceeds to prepay the term loans maturing in March 2013.

On October 1, 2012, we acquired J.A. Thomas and Associates, Inc. ("JA Thomas"), the nation's premier provider of physician-oriented, clinical documentation improvement programs for the healthcare industry, for approximately \$265.0 million, of which \$240.0 million was paid in cash at the closing, and the remaining \$25.0 million is payable in cash or shares of our common stock, at our election, on the second anniversary of the closing date, subject to certain adjustments and conditions.

We believe our current cash and cash equivalents are sufficient to meet our operating needs for at least the next twelve months.

Cash provided by operating activities

Fiscal 2012 Compared to Fiscal 2011

Cash provided by operating activities for fiscal 2012 was \$473.0 million, an increase of \$115.6 million, or 32%, as compared to cash provided by operating activities of \$357.4 million for fiscal 2011. The increase was primarily driven by the following factors:

• An increase of \$89.8 million in cash flows resulting from higher net income, exclusive of non-cash adjustment items which includes deferred tax benefit of \$151.5 million driven by the release of our valuation allowance;

• An increase of \$42.5 million in cash flows generated by changes in working capital excluding deferred revenue, primarily driven by a onetime payment of €18.0 million (\$23.4 million equivalent) during the first quarter of fiscal 2011 for a fixed obligation assumed in connection with our acquisition of SpinVox and a \$30.8 million increase in cash flows due to changes in accounts payable; and

• A decrease in cash flows of \$16.8 million from deferred revenue.

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Fiscal 2011 Compared to Fiscal 2010

Cash provided by operating activities for fiscal 2011 was \$357.4 million, an increase of \$61.1 million, or 21%, as compared to cash provided by operating activities of \$296.3 million for fiscal 2010. The increase was primarily driven by the following factors:

An increase of \$90.0 million in cash flows resulting from an increase in net income, exclusive of non-cash adjustment items which include a one-time non-cash tax benefit adjustment of \$34.7 million reducing the valuation allowance on deferred tax assets as a result of the Equitrac acquisition;

An increase in cash flows of \$16.8 million from an overall increase in deferred revenue; and

A decrease of \$45.6 million in cash flows generated by changes in working capital excluding deferred revenue, primarily driven by an €18.0 million (\$23.4 million equivalent) payment in fiscal 2011 for a fixed obligation assumed in connection with our acquisition of SpinVox and a \$24.8 million decrease in cash flows due to changes in accounts receivable.

Cash used in investing activities

Fiscal 2012 compared to Fiscal 2011

Cash used in investing activities for fiscal 2012 was \$924.5 million, an increase of \$498.6 million, or 117%, as compared to cash used in investing activities of \$425.9 million for fiscal 2011. The net increase was primarily driven by the following factors:

An increase in cash outflows of \$475.9 million for business and technology acquisitions, primarily driven by the cash consideration paid in connection with our acquisitions in fiscal 2012; and

An increase in cash outflows of \$28.0 million resulting from additional capital expenditure, primarily related to the purchase of a corporate asset during fiscal 2012.

Fiscal 2011 compared to Fiscal 2010

Cash used in investing activities for fiscal 2011 was \$425.9 million, an increase of \$110.3 million or 35%, as compared to cash used in investing activities of \$315.6 million for fiscal 2010. The net increase was primarily driven by the following factors:

An increase in cash outflows of \$198.6 million for acquisitions in fiscal 2011 as compared to fiscal 2010;

A decrease in net cash outflows of \$34.4 million to purchase marketable securities net of proceeds; and

A decrease in cash outflows of \$39.3 million related to restricted cash. During fiscal 2011, we received \$17.2 million in cash upon satisfaction of the restriction of our restricted cash. During fiscal 2010, we used \$22.1 million for an irrevocable standby letter of credit account for a fixed obligation in connection with our acquisition of SpinVox in 2010.

Cash provided by financing activities

Fiscal 2012 compared to Fiscal 2011

Cash provided by financing activities for fiscal 2012 was \$1,133.0 million, an increase of \$1,127.0 million, or 18,783%, as compared to cash provided by financing activities of \$6.0 million for fiscal 2011. The change was primarily driven by the following factors:

A \$689.1 million cash inflow resulting from the issuance of the Senior Notes due 2020, net of issuance costs in August 2012;

A \$676.1 million cash inflow resulting from the issuance of the 2031 Debentures, net of issuance costs, offset by \$200.0 million that we used to repurchase 8.5 million shares of our common stock in October 2011;

Offset by a decrease of \$21.1 million cash benefit resulting from excess tax benefits on employee equity awards; and

An increase in cash outflows of \$13.0 million as a result of higher cash payments required to net share settle employee equity awards, due to an increase in the number of shares vested and an increase in the intrinsic value of the shares vested as a result of the overall increase in our stock price in fiscal 2012 as compared to fiscal 2011.

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Fiscal 2011 compared to Fiscal 2010

Cash provided by financing activities for fiscal 2011 was \$6.0 million, a decrease of \$3.9 million, or 39%, as compared to cash provided by financing activities of \$9.9 million for fiscal 2010. The change was primarily driven by the following factors:

- An increase of \$16.5 million cash benefit resulting from excess tax benefits on employee equity awards;
- An increase in cash outflows of \$14.9 million to net share settle employee equity awards, due to an increase in the number of shares vested and an increase in the intrinsic value of the shares vested as a result of the overall increase in our stock price in fiscal 2011 as compared to fiscal 2010; and
- A decrease in cash inflows of \$12.4 million from the sale of our common stock. During fiscal 2010, warrants to purchase 2.5 million of our shares were exercised, whereas we had no warrant activity in fiscal 2011.

Credit Facilities and Debt

5.375% Senior Notes due 2020

On August 14, 2012, we issued \$700 million aggregate principal amount of 5.375% Senior Notes (the "Notes") in a private placement due on August 15, 2020. The proceeds from the Notes were approximately \$689.1 million, net of issuance costs. The Notes bear interest at 5.375% per year, payable in cash semi-annually in arrears, beginning on February 15, 2013.

The Notes are the unsecured senior obligations of the Company and are guaranteed (the "Guarantees") on an unsecured senior basis by substantially all of the Company's direct and indirect wholly owned domestic subsidiaries (the "Subsidiary Guarantors"). The Notes and Guarantees rank equally in right of payment with all of the Company's and the Subsidiary Guarantors' existing and future unsecured senior debt and rank senior in right of payment to all of the Company's and the Subsidiary Guarantors' future unsecured subordinated debt. The Notes and Guarantees effectively rank junior to all secured debt of the Company and the Subsidiary Guarantors to the extent of the value of the collateral securing such debt and to all liabilities, including trade payables, of the Company's subsidiaries that have not guaranteed the Notes.

At any time before August 15, 2016, we may redeem all or a portion of the Notes at a redemption price equal to 100% of the aggregate principal amount of the Notes to be redeemed, plus a "make-whole" premium and accrued and unpaid interest to, but excluding, the redemption date. At any time on or after August 15, 2016, we may redeem all or a portion of the Notes at certain redemption prices expressed as percentages of the principal amount, plus accrued and unpaid interest to, but excluding, the redemption date. At any time and from time to time before August 15, 2015, we may redeem up to 35% of the aggregate outstanding principal amount of the Notes with the net cash proceeds received by the Company from certain equity offerings at a price equal to 105.375%, plus accrued and unpaid interest to, but excluding, the redemption date, provided that the redemption occurs no later than the 120 day after the closing of the related equity offering, and at least 50% of the original aggregate principal amount of the Notes remains outstanding immediately thereafter.

Upon the occurrence of certain asset sales or a change in control, we must offer to repurchase the Notes at a price equal to 100%, in the case of an asset sale, or 101%, in the case of a change of control, of the principal amount plus accrued and unpaid interest to, but excluding, the repurchase date.

2.75% Convertible Debentures due in 2031

On October 24, 2011, we sold \$690 million of 2.75% Convertible Debentures due in 2031 (the "2031 Debentures") in a private placement. Total proceeds, net of debt issuance costs, were \$676.1 million. The 2031 Debentures bear interest at 2.75% per year, payable in cash semiannually in arrears, beginning on May 1, 2012. The 2031 Debentures mature on November 1, 2031, subject to the right of the holders to require us to redeem the 2031 Debentures on November 1, 2017, 2021, and 2026. The 2031 Debentures are general senior unsecured obligations and rank equally in right of payment with all of our existing and future unsecured, unsubordinated indebtedness and senior in right of payment to any indebtedness that is contractually subordinated to the 2031 Debentures. The 2031 Debentures will be effectively

subordinated to indebtedness and other liabilities of our subsidiaries.

If converted, the principal amount of the 2031 Debentures is payable in cash and any amounts payable in excess of the \$690 million principal amount, will (based on an initial conversion rate, which represents an initial conversion price of approximately \$32.30 per share, subject to adjustment) be paid in cash or shares of our common stock, at our election, only in the following circumstances and to the following extent: (i) on any date during any fiscal quarter beginning after December 31, 2011 (and only during such fiscal quarter) if the closing sale price of our common stock was more than 130% of the then current conversion price for at least 20 trading days in the period of the 30 consecutive trading days ending on the last trading day of the

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previous fiscal quarter; (ii) during the five consecutive business-day period following any five consecutive trading-day period in which the trading price for \$1,000 principal amount of the Debentures for each day during such five trading-day period was less than 98% of the closing sale price of our common stock multiplied by the then current conversion rate; (iii) upon the occurrence of specified corporate transactions, as described in the indenture for the 2031 Debentures; or (iv) at the option of the holder at any time on or after May 1, 2031. Additionally, we may redeem the 2031 Debentures, in whole or in part, on or after November 6, 2017 at par plus accrued and unpaid interest. Each holder shall have the right, at such holder's option, to require us to repurchase all or any portion of the 2031 Debentures held by such holder on November 1, 2017, November 1, 2021, and November 1, 2026 at par plus accrued and unpaid interest. Upon conversion, we will pay the principal amount in cash and any amounts payable in excess of the \$690 million principal amount will be paid in cash or shares of our common stock, at our election. If we undergo a fundamental change (as described in the indenture for the 2031 Debentures) prior to maturity, holders will have the option to require us to repurchase all or any portion of their debentures for cash at a price equal to 100% of the principal amount of the debentures to be purchased plus any accrued and unpaid interest, including any additional interest to, but excluding, the repurchase date. As of September 30, 2012, no conversion triggers were met. If the conversion triggers were met, we could be required to repay all or some of the principal amount in cash prior to the maturity date.

2.75% Convertible Debentures due in 2027

We have \$250 million of 2.75% convertible senior debentures due in 2027 (“the 2027 Debentures”) that were issued on August 13, 2007 in a private placement to Citigroup Global Markets Inc. and Goldman, Sachs & Co. The 2027 Debentures bear an interest rate of 2.75% per annum, payable semi-annually in arrears beginning on February 15, 2008, and mature on August 15, 2027 subject to the right of the holders of the 2027 Debentures to require us to redeem the 2027 Debentures on August 15, 2014, 2017 and 2022. The 2027 Debentures are general senior unsecured obligations, ranking equally in right of payment to all of our existing and future unsecured, unsubordinated indebtedness and senior in right of payment to any indebtedness that is contractually subordinated to the 2027 Debentures. The 2027 Debentures are effectively subordinated to our secured indebtedness to the extent of the value of the collateral securing such indebtedness and are structurally subordinated to indebtedness and other liabilities of our subsidiaries. If converted, the principal amount of the 2027 Debentures is payable in cash and any amounts payable in excess of the \$250 million principal amount, will (based on an initial conversion rate, which represents an initial conversion price of approximately \$19.47 per share, subject to adjustment as defined therein) be paid in cash or shares of our common stock, at our election, only in the following circumstances and to the following extent: (i) on any date during any fiscal quarter beginning after September 30, 2007 (and only during such fiscal quarter) if the closing sale price of our common stock was more than 120% of the then current conversion price for at least 20 trading days in the period of the 30 consecutive trading days ending on the last trading day of the previous fiscal quarter; (ii) during the five consecutive business-day period following any five consecutive trading-day period in which the trading price for \$1,000 principal amount of the Debentures for each day during such five trading-day period was less than 98% of the closing sale price of our common stock multiplied by the then current conversion rate; (iii) upon the occurrence of specified corporate transactions, as described in the indenture for the 2027 Debentures; and (iv) at the option of the holder at any time on or after February 15, 2027. Additionally, we may redeem the 2027 Debentures, in whole or in part, on or after August 20, 2014 at par plus accrued and unpaid interest. Each holder shall have the right, at such holder's option, to require us to repurchase all or any portion of the 2027 Debentures held by such holder on August 15, 2014, August 15, 2017 and August 15, 2022 at par plus accrued and unpaid interest. Upon conversion, we will pay the principal amount in cash and any amounts payable in excess of the \$250 million principal amount will be paid in cash or shares of our common stock, at our election. If we undergo a fundamental change (as described in the indenture for the 2027 Debentures) prior to maturity, holders will have the option to require us to repurchase all or any portion of their debentures for cash at a price equal to 100% of the principal amount of the debentures to be purchased plus any accrued and unpaid interest, including any additional interest to, but excluding, the repurchase date.

Our stock price exceeded the conversion threshold price of \$23.36 per share for at least 20 days during the 30 consecutive trading days ended September 30, 2012. Accordingly, the 2027 Debentures will be convertible at the

holders' option during the quarter ended December 31, 2012 and therefore are classified as current liabilities at September 30, 2012. Given that the debentures are traded in a secondary market and the current market value of the 2027 Debentures exceeds the value that the holders would receive upon conversion, we believe that the holders may not have a significant economic incentive to exercise their conversion option prior to August 2014. As a result, we do not expect a material amount of the 2027 Debentures to be redeemed in the three months ended December 31, 2012. The difference between the carrying value of the 2027 Debentures and the \$250.0 million principal amount reflects the unamortized portion of the original issue discount recognized upon issuance of the notes, which is being amortized over the expected term of the convertible debt. Because the 2027 Debentures were convertible at September 30, 2012, an amount equal to the 18.4 million unamortized portion of the original issue discount was separately classified in our consolidated balance sheets as temporary equity and referred to as "Equity component of currently redeemable convertible debentures."

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Credit Facility

Our credit facility consists of a \$75 million revolving credit line including letters of credit, a \$355 million term loan entered into on March 31, 2006, a \$90 million term loan entered into on April 5, 2007 and a \$225 million term loan entered into on August 24, 2007 (the "Credit Facility"). In July 2011, we entered into agreements to amend and restate our existing Credit Facility. Of the approximately \$638.5 million remaining term loan as of July 1, 2011, lenders representing \$493.2 million elected to extend the maturity date by three years to March 31, 2016. The remaining term loans retained the original maturity date of March 2013. In addition, lenders participating in the revolving credit facility have chosen to extend the maturity date by three years to March 31, 2015. As of September 30, 2012, \$630.6 million remained outstanding under the term loans, there were \$17.9 million of letters of credit issued under the revolving credit line and there were no other outstanding borrowings under the revolving credit line. On October 31, 2012, we paid the remaining outstanding term loans balance of \$143.5 million originally maturing March 2013.

The Credit Facility contains covenants, including, among other things, covenants that restrict our ability and those of our subsidiaries to incur certain additional indebtedness, create or permit liens on assets, enter into sale-leaseback transactions, make loans or investments, sell assets, make certain acquisitions, pay dividends, or repurchase stock. The agreement also contains events of default, including failure to make payments of principal or interest, failure to observe covenants, breaches of representations and warranties, defaults under certain other material indebtedness, failure to satisfy material judgments, a change of control and certain insolvency events. As of September 30, 2012, we were in compliance with the covenants under the Credit Facility.

Under terms of the amended Credit Agreement, interest is payable monthly at a rate equal to the applicable margin plus, at our option, either (a) the base rate which is the higher of the corporate base rate of UBS AG, Stamford Branch, or the federal funds rate plus 0.50% per annum or (b) LIBOR (equal to (i) the British Bankers' Association Interest Settlement Rates for deposits in U.S. dollars divided by (ii) one minus the statutory reserves applicable to such borrowing). The applicable margin for the borrowings is as follows:

Description	Base Rate Margin	LIBOR Margin
Term loans maturing March 2013	0.75% - 1.50%(a)	1.75% - 2.50%(a)
Term loans maturing March 2016	2.00%	3.00%
Revolving facility due March 2015	1.25% - 2.25%(b)	2.25% - 3.25%(b)

(a) The margin is determined based on our leverage ratio and credit rating at the date the interest rates are reset on the Term Loans.

(b) The margin is determined based on our leverage ratio and credit rating at the date the interest rates are reset on the Revolving credit line.

At September 30, 2012 the applicable margins were 2.00%, with an effective rate of 2.24%, on the remaining balance of \$143.5 million maturing in March 2013 and 3.00%, with an effective rate of 3.24%, on the remaining balance of \$487.1 million maturing in March 2016. We are required to pay a commitment fee for unutilized commitments under the revolving credit facility at a rate ranging from 0.375% to 0.50% per annum, based upon our leverage ratio. As of September 30, 2012, the commitment fee rate was 0.375%.

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Principal payments on the extended loan are due in quarterly installments of 0.25% of the then outstanding balance through March 2016, at which point the remaining balance becomes due. In addition, an annual excess cash flow sweep, as defined in the Credit Facility, is payable in the first quarter of each fiscal year, based on the excess cash flow generated in the previous fiscal year. We have not generated excess cash flows in any period and no additional payments are required. We will continue to evaluate the extent to which a payment is due in the first quarter of future fiscal years based on excess cash flow generation. At the current time, we are unable to predict the amount of the outstanding principal, if any, that may be required to be repaid in future fiscal years pursuant to the excess cash flow sweep provisions. Any term loan borrowings not paid through the baseline repayment, the excess cash flow sweep, or any other mandatory or optional payments that we may make, will be repaid upon maturity. If only the baseline repayments are made, the annual aggregate principal amount of the term loans repaid would be as follows (dollars in thousands):

Year Ending September 30,	Amount
2013	148,385
2014	4,804
2015	4,756
2016	472,651
Total	\$630,596

Our obligations under the Credit Facility are unconditionally guaranteed by, subject to certain exceptions, each of our existing and future direct and indirect wholly-owned domestic subsidiaries. The Credit Facility and the guarantees thereof are secured by first priority liens and security interests in the following: 100% of the capital stock of substantially all of our domestic subsidiaries and 65% of the outstanding voting equity interests and 100% of the non-voting equity interests of first-tier foreign subsidiaries, all our material tangible and intangible assets and those of the guarantors, and any present and future intercompany debt. The Credit Facility also contains provisions for mandatory prepayments of outstanding term loans upon receipt of the following, and subject to certain exceptions: 100% of net cash proceeds from asset sales, 100% of net cash proceeds from issuance or incurrence of debt, and 100% of extraordinary receipts. We may voluntarily prepay borrowings under the Credit Facility without premium or penalty other than breakage costs, as defined with respect to LIBOR-based loans.

We believe that cash flows from future operations in addition to cash and cash equivalents on-hand will be sufficient to meet our working capital, investing, financing and contractual obligations and the contingent payments for acquisitions, if any are realized, as they become due for at least the next twelve months. We also believe that in the event future operating results are not as planned, that we could take actions, including restructuring actions and other cost reduction initiatives, to reduce operating expenses to levels which, in combination with expected future revenue, will continue to generate sufficient operating cash flow. In the event that these actions are not effective in generating operating cash flows we may be required to issue equity or debt securities on terms that may be less favorable.

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Off-Balance Sheet Arrangements, Contractual Obligations, Contingent Liabilities and Commitments

Contractual Obligations

The following table outlines our contractual payment obligations as of September 30, 2012 (dollars in millions):

Contractual Obligations	Payments Due by Fiscal Year Ended September 30,				
	Total	2013	2014 and 2015	2016 and 2017	Thereafter
Credit Facility(1)	\$630.6	\$148.4	\$9.6	\$472.6	\$—
Convertible Debentures(2)	940.0	—	250.0	—	690.0
Senior Notes	700.0	—	—	—	700.0
Interest payable on long-term debt(3)	462.1	80.7	150.9	120.8	109.7
Letter of Credit(4)	17.9	17.9	—	—	—
Operating leases	120.1	28.0	43.7	34.0	14.4
Purchase commitments for inventory, property and equipment(5)	6.5	6.5	—	—	—
Collaboration agreements(6)	30.9	23.4	7.5	—	—
Other long-term liabilities assumed(7)	8.5	2.5	5.0	1.0	—
Deferred acquisition payments	27.9	27.9	—	—	—
Total contractual cash obligations	\$2,944.5	\$335.3	\$466.7	\$628.4	\$1,514.1

(1) Principal is paid on a quarterly basis under the Credit Facility.

Holder of the 2027 Debentures have the right to require us to repurchase the debentures on August 15, 2014, 2017 (2) and 2022. Holders of the 2031 Debentures have the right to require us to redeem the Debentures on November 1, 2017, 2021, and 2026.

Interest on the Credit Facility is due and payable monthly and is estimated using the effective interest rate as of (3) September 30, 2012. Interest is due and payable semi-annually under 2027 Debentures and 2031 Debentures at a rate of 2.75%. Interest is due and payable semi-annually on the Senior notes at a rate of 5.375%.

(4) Letters of Credit are in place primarily to secure future operating lease payments.

(5) These amounts include non-cancelable purchase commitments for inventory in the normal course of business to fulfill customers' orders currently scheduled in our backlog.

(6) Payments under the research collaboration agreements are payable in cash or common stock at our option.

Obligations include assumed long-term liabilities relating to restructuring program initiated by a previous acquisition in 2003. The restructuring program related to the closing of a facility with lease term set to expire in 2016. Total contractual obligation under the lease is \$8.5 million. As of September 30, 2012, we have sub-leased (7) certain of the office space related to the facility to unrelated third parties. Total sublease income under contractual terms is expected to be \$5.3 million, which ranges from \$0.7 million to \$1.6 million on an annualized basis through 2016.

The gross liability for unrecognized tax benefits as of September 30, 2012 was \$17.4 million. We do not expect a significant change in the amount of unrecognized tax benefits within the next 12 months. We estimate that none of this amount will be paid within the next year and we are currently unable to reasonably estimate the timing of payments for the remainder of the liability.

Contingent Liabilities and Commitments

In connection with our acquisition of Swype, Inc. in October 2011, we agreed to make deferred payments to the former shareholders of Swype of up to \$25.0 million in April 2013, contingent upon the continued employment of

three named executives and certain other conditions. The contingent payments will be reduced by amounts specified in the merger agreement in the event that any of the three executives terminates employment prior to the payment date or if any losses occur to which we would be entitled to indemnification under the merger agreement.

In connection with our acquisition of Vocada, Inc. in November 2007, we agreed to make contingent earn-out payments of up to \$21.0 million upon the achievement of certain financial targets measured over defined periods through December 31, 2010. We have notified the former shareholders of Vocada that the financial targets were not achieved. In December 2010, the former shareholders filed a demand for arbitration in accordance with their rights under the merger agreement. On October 4, 2012, the

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arbitration panel issued its conclusion indicating that no additional payments to the former shareholders under the Vocada agreement are required. Vocada shareholders have filed a motion to vacate this ruling. At September 30, 2012, we have not recorded any obligation related to the Vocada earn-out provisions.

Financial Instruments

We use financial instruments to manage our foreign exchange risk. We follow Financial Accounting Standards Board Accounting Standards Codification 815 (“ASC 815”), Derivatives and Hedging, for our derivative instruments.

We operate our business in countries throughout the world and transact business in various foreign currencies. Our foreign currency exposures typically arise from transactions denominated in currencies other than the local functional currency of our operations. We have a program that primarily utilizes foreign currency forward contracts to offset the risks associated with foreign currency denominated assets and liabilities. We established this program so that gains and losses from remeasurement or settlement of these assets and liabilities are offset by gains or losses on the foreign currency forward contracts thus mitigating the risks and volatility associated with our foreign currency transactions. Generally, we enter into contracts with terms of 90 days or less, and at September 30, 2012 we had outstanding contracts with a total notional value of \$83.9 million.

From time to time we will enter into agreements that allow us to issue shares of our common stock as part or all of the consideration related to partnering and technology acquisition activities. Generally these shares are issued subject to security price guarantees which are accounted for as derivatives. We have determined that these instruments would not be considered equity instruments if they were freestanding. The security price guarantees require payment from either us to the third party, or from the third party to us, based upon the difference between the price of our common stock on the issue date and an average price of our common stock approximately six months following the issue date. Changes in the fair value of these security price guarantees are reported in earnings in each period as non-operating income (expense) with other income, net. During the year ended September 30, 2012 and 2011, we recorded \$8.0 million and \$13.2 million, respectively of gains associated with these contracts and received cash payments totaling \$9.0 million and \$9.4 million, respectively, upon to settlement of the agreements during the year.

Pension Plans

In connection with our acquisition of Dictaphone in March 2006, we assumed the defined benefit pension plans for former Dictaphone employees located in the United Kingdom and Canada. These two pension plans are closed to new participants and require periodic cash contributions. In fiscal 2012, total cash funding for the UK pension plan was \$1.3 million. For the UK pension plan, we have a minimum funding requirement of £0.7 million (approximately \$1.1 million based on the exchange rate at September 30, 2012) for fiscal 2013. We have announced a plan to terminate the Canadian pension plan and do not expect to make any significant additional contributions to settle the obligations of the plan.

In connection with our acquisition of SVOX A.G. in June 2011, we assumed an additional defined benefit pension plan for employees in Switzerland. At the end of September, 2012, the plan benefit obligations exceed the plan assets by approximately \$1.4 million. The plan requires periodic cash contributions, including participant contributions from active employees. Company contributions in fiscal 2013 are expected to be \$0.2 million.

Off-Balance Sheet Arrangements

Through September 30, 2012, we have not entered into any off-balance sheet arrangements or material transactions with unconsolidated entities or other persons.

CRITICAL ACCOUNTING POLICIES, JUDGMENTS AND ESTIMATES

The preparation of financial statements in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. On an ongoing basis, we evaluate our estimates, assumptions and judgments, including those related to revenue recognition; allowance for doubtful accounts and returns; the valuation of goodwill, intangible assets and tangible long-lived assets; accounting for business combinations; accounting for stock-based compensation; accounting for derivative instruments; accounting for income taxes and related valuation allowances; and loss contingencies. Our management bases its estimates on historical experience, market participant fair value considerations and various other factors that are believed to be reasonable under the circumstances. Actual results could differ from these estimates.

We believe the following critical accounting policies most significantly affect the portrayal of our financial condition and

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results of operations and require our most difficult and subjective judgments.

Revenue Recognition. We derive revenue from the following sources: (1) software license agreements, including royalty and other usage-based arrangements, (2) professional services, (3) hosting services and (4) post-contract customer support ("PCS"). Our hosting services are generally provided through on-demand, usage-based or per transaction fee arrangements. Our revenue recognition policies for these revenue streams are discussed below.

The sale and/or license of software products and technology is deemed to have occurred when a customer either has taken possession of or has access to take immediate possession of the software or technology. In select situations, we sell or license intellectual property in conjunction with, or in place of, embedding our intellectual property in software. We also have non-software arrangements including hosting services where the customer does not take possession of the software at the outset of the arrangement either because they have no contractual right to do so or because significant penalties preclude them from doing so. Generally we recognize revenue when (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable and (iv) collectibility is probable.

Revenue from royalties on sales of our software products by original equipment manufacturers ("OEMs"), where no services are included, is recognized in the quarter earned so long as we have been notified by the OEM that such royalties are due, and provided that all other revenue recognition criteria are met.

Software arrangements generally include PCS, which includes telephone support and the right to receive unspecified upgrades/enhancements on a when-and-if-available basis, typically for one to five years. Revenue from PCS is recognized ratably on a straight-line basis over the term that the maintenance service is provided. When PCS renews automatically, we provide a reserve based on historical experience for contracts expected to be canceled for non-payment. All known and estimated cancellations are recorded as a reduction to revenue and accounts receivable.

For our software and software-related multiple element arrangements, where customers purchase both software related products and software related services, we use vendor-specific objective evidence ("VSOE") of fair value for software and software-related services to separate the elements and account for them separately. VSOE exists when a company can support what the fair value of its software and/or software-related services is based on evidence of the prices charged when the same elements are sold separately. VSOE of fair value is required, generally, in order to separate the accounting for various elements in a software and related services arrangement. We have established VSOE of fair value for the majority of our PCS, professional services, and training.

When we provide professional services considered essential to the functionality of the software, we recognize revenue from the professional services as well as any related software licenses on a percentage-of-completion basis whereby the arrangement consideration is recognized as the services are performed, as measured by an observable input. In these circumstances, we separate license revenue from professional service revenue for income statement presentation by allocating VSOE of fair value of the professional services as professional services and hosting revenue and the residual portion as product and licensing revenue. We generally determine the percentage-of-completion by comparing the labor hours incurred to-date to the estimated total labor hours required to complete the project. We consider labor hours to be the most reliable, available measure of progress on these projects. Adjustments to estimates to complete are made in the periods in which facts resulting in a change become known. When the estimate indicates that a loss will be incurred, such loss is recorded in the period identified. Significant judgments and estimates are involved in determining the percent complete of each contract. Different assumptions could yield materially different results.

We offer some of our products via a Software-as-a-Service ("SaaS") model also known as a hosted model. In this type of arrangement, we are compensated in two ways: (1) fees for up-front set-up of the service environment and (2) fees charged on a usage or per transaction basis. Our up-front set-up fees are nonrefundable. We recognize the up-front

set-up fees ratably over the longer of the contract lives, or the expected lives of the customer relationships. The on-demand, usage-based or per transaction fees are due and payable as each individual transaction is processed through the hosted service and is recognized as revenue in the period the services are provided.

We enter into multiple-element arrangements that may include a combination of our various software related and non-software related products and services offerings including software licenses, PCS, professional services, and our hosting services. In such arrangements we allocate total arrangement consideration to software or software-related elements and any non-software element separately based on the selling price hierarchy group following the guidance in Accounting Standards Codification ("ASC") 985-605, Software Revenue Recognition and our policies. We determine the selling price for each deliverable using VSOE of selling price, if it exists, or Third Party Evidence ("TPE") of selling price. Typically, we are unable to determine TPE of selling price. Therefore, when neither VSOE nor TPE of selling price exist for a deliverable, we use our Estimate of Selling Price ("ESP") for the purposes of allocating the arrangement consideration. We determine ESP for a product or service by considering multiple

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factors including, but not limited to, major project groupings, market conditions, competitive landscape, price list and discounting practices. Revenue allocated to each element is then recognized when the basic revenue recognition criteria are met for each element.

When products are sold through distributors or resellers, title and risk of loss generally passes upon shipment, at which time the transaction is invoiced and payment is due. Shipments to distributors and resellers without right of return are recognized as revenue upon shipment, provided all other revenue recognition criteria are met. Certain distributors and resellers have been granted rights of return for as long as the distributors or resellers hold the inventory. We cannot estimate historical returns from these distributors and resellers; and therefore, cannot use such estimates as the basis upon which to estimate future sales returns. As a result, we recognize revenue from sales to these distributors and resellers when the products are sold through to retailers and end-users.

When products are sold directly to retailers or end-users, we make an estimate of sales returns based on historical experience. The provision for these estimated returns is recorded as a reduction of revenue and accounts receivable at the time that the related revenue is recorded. If actual returns differ significantly from our estimates, such differences could have a material impact on our results of operations for the period in which the actual returns become known.

We record consideration given to a reseller as a reduction of revenue to the extent we have recorded cumulative revenue from the customer or reseller. However, when we receive an identifiable benefit in exchange for the consideration, and can reasonably estimate the fair value of the benefit received, the consideration is recorded as an operating expense.

We record reimbursements received for out-of-pocket expenses as revenue, with offsetting costs recorded as cost of revenue. Out-of-pocket expenses generally include, but are not limited to, expenses related to transportation, lodging and meals. We record shipping and handling costs billed to customers as revenue with offsetting costs recorded as cost of revenue.

Our revenue recognition policies require management to make significant estimates. Management analyzes various factors, including a review of specific transactions, historical experience, creditworthiness of customers and current market and economic conditions. Changes in judgments based upon these factors could impact the timing and amount of revenue and cost recognized and thus affects our results of operations and financial condition.

Business Combinations. We determine and allocate the purchase price of an acquired company to the tangible and intangible assets acquired and liabilities assumed as of the business combination date. The purchase price allocation process requires us to use significant estimates and assumptions, including fair value estimates, as of the business acquisition date, including:

- estimated fair values of intangible assets;
- estimated fair market values of legal performance commitments to customers, assumed from the acquiree under existing contractual obligations (classified as deferred revenue) at the date of acquisition;
- estimated fair market values of stock awards assumed from the acquiree that are included in the purchase price;
- estimated fair market value of required payments under contingent consideration provisions;
- estimated income tax assets and liabilities assumed from the acquiree; and
- estimated fair value of pre-acquisition contingencies assumed from the acquiree.

While we use our best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the business combination date, our estimates and assumptions are inherently uncertain and subject to refinement. As a result, during the purchase price allocation period, which is generally one

year from the business combination date, we record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. For changes in the valuation of intangible assets between preliminary and final purchase price allocation, the related amortization is adjusted effective from the acquisition date. Subsequent to the purchase price allocation period any adjustment to assets acquired or liabilities assumed is included in operating results in the period in which the adjustment is determined.

Although we believe the assumptions and estimates we have made in the past have been reasonable and appropriate, they are based in part on historical experience and information obtained from the management of the acquired companies and are inherently uncertain. Examples of critical estimates in valuing certain of the intangible assets we have acquired or may acquire in the future include but are not limited to:

future expected cash flows from software license sales, support agreements, consulting contracts, other customer

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contracts and acquired developed technologies and patents;
• expected costs to develop in-process research and development projects into commercially viable products and the estimated cash flows from the projects when completed;
• the acquired company's brand and competitive position, as well as assumptions about the period of time the acquired brand will continue to be used in the combined company's product portfolio; and
• discount rates.

Unanticipated events and circumstances may occur which may affect the accuracy or validity of such assumptions, estimates or actual results.

In connection with the purchase price allocations for our acquisitions, we estimate the fair market value of legal performance commitments to customers, which are classified as deferred revenue. The estimated fair market value of these obligations is determined and recorded as of the acquisition date.

For a given acquisition, we may identify certain pre-acquisition contingencies. If, during the purchase price allocation period, we are able to determine the fair value of a pre-acquisition contingency, we will include that amount in the purchase price allocation. If we are unable to determine the fair value of a pre-acquisition contingency at the end of the purchase price allocation period, we will evaluate whether to include an amount in the purchase price allocation based on whether it is probable a liability had been incurred and whether an amount can be reasonably estimated. After the end of the purchase price allocation period, any adjustment to amounts recorded for a pre-acquisition contingency will be included in our operating results in the period in which the adjustment is determined.

Goodwill, Intangible and Other Long-Lived Assets and Impairment Assessments. We have significant long-lived tangible and intangible assets, including goodwill and intangible assets with indefinite lives, which are susceptible to valuation adjustments as a result of changes in various factors or conditions. The most significant finite-lived tangible and intangible assets are customer relationships, licensed technology, patents and core technology, completed technology, fixed assets and trade names. All finite-lived intangible assets are amortized over the estimated economic lives of the assets, generally using the straight-line method except where the pattern of the expected economic benefit is readily identifiable, primarily customer relationship intangibles, whereby amortization follows that pattern. The values of intangible assets determined in connection with a business combination, with the exception of goodwill, were initially determined by a risk-adjusted, discounted cash flow approach. We assess the potential impairment of intangible and fixed assets whenever events or changes in circumstances indicate that the carrying values may not be recoverable. Goodwill and indefinite-lived intangible assets are assessed for potential impairment at least annually, but also whenever events or changes in circumstances indicate the carrying values may not be recoverable. Factors we consider important, which could trigger an impairment of such assets, include the following:

- significant underperformance relative to historical or projected future operating results;
- significant changes in the manner of or use of the acquired assets or the strategy for our overall business;
- significant negative industry or economic trends;
- significant decline in our stock price for a sustained period; and
- a decline in our market capitalization below net book value.

Future adverse changes in these or other unforeseeable factors could result in an impairment charge that would materially impact future results of operations and financial position in the reporting period identified.

We test goodwill and intangible assets with indefinite lives for impairment annually in the fourth quarter, and between annual tests if indicators of potential impairment exist. The impairment test for goodwill and intangible assets with indefinite lives compares the fair value of identified reporting unit(s) to its (their) carrying amount to assess whether such assets are impaired. We have seven reporting units based on the level of information provided to, and review

thereof, by our segment management.

We determine fair values for each of the reporting units using an income approach. When available and appropriate, we also use a comparative market approach to derive the fair values. For purposes of the income approach, fair value is determined based on the present value of estimated future cash flows, discounted at an appropriate risk adjusted rate. We use our internal forecasts to estimate future cash flows and include an estimate of long-term future growth rates based on our most recent views of the long-term outlook for each business. Actual results may differ from those assumed in our forecasts. We derive our discount rates using a capital asset pricing model and analyzing published rates for industries relevant to our reporting units to estimate the cost of

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equity financing. We use discount rates that are commensurate with the risks and uncertainty inherent in the respective businesses and in our internally developed forecasts. Discount rates used in our reporting unit valuations ranged from 12% to 21%. For purposes of the market approach, we use a valuation technique in which values are derived based on market prices of comparable publicly traded companies. We also use a market based valuation technique in which values are determined based on relevant observable information generated by market transactions involving comparable businesses. Compared to the market approach, the income approach more closely aligns each reporting unit valuation to our business profile, including geographic markets served and product offerings. Required rates of return, along with uncertainty inherent in the forecasts of future cash flows, are reflected in the selection of the discount rate. Equally important, under this approach, reasonably likely scenarios and associated sensitivities can be developed for alternative future states that may not be reflected in an observable market price. A market approach allows for comparison to actual market transactions and multiples. It can be somewhat more limited in its application because the population of potential comparable entities is often limited to publicly-traded companies where the characteristics of the comparative business and ours can be significantly different, market data is usually not available for divisions within larger conglomerates or non-public subsidiaries that could otherwise qualify as comparable, and the specific circumstances surrounding a market transaction (e.g., synergies between the parties, terms and conditions of the transaction, etc.) may be different or irrelevant with respect to our business. It can also be difficult, under certain market conditions, to identify orderly transactions between market participants in similar businesses. We assess each valuation methodology based upon the relevance and availability of the data at the time we perform the valuation and weight the methodologies appropriately.

The carrying values of the reporting units were determined based on an allocation of our assets and liabilities through specific allocation of certain assets and liabilities, to the reporting units and an apportionment method based on relative size of the reporting units' revenues and operating expenses compared to the Company as a whole. Goodwill was initially allocated to our reporting units based on the relative fair value of the units at the date we implemented the current reporting unit structure. Goodwill subsequently acquired through acquisitions is allocated to the applicable reporting unit based upon the relative fair value of the acquired business. Certain corporate assets that are not instrumental to the reporting units' operations and would not be transferred to hypothetical purchasers of the reporting units were excluded from the reporting units' carrying values.

Based on our assessments, we have not had any impairment charges during our history as a result of our impairment evaluation of goodwill. Significant adverse changes in our future revenues and/or cash flow results, or significant degradation in the enterprise values of comparable companies within our segments, could result in the determination that all or a portion of our goodwill is impaired. However, as of our fiscal 2012 annual impairment assessment date, our estimated fair values of our reporting units significantly exceeded their carrying values.

We periodically review long-lived assets other than goodwill or indefinite-lived intangible assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable or that the useful lives of those assets are no longer appropriate. Each impairment test is based on a comparison of the undiscounted cash flows to the recorded carrying value for the asset or asset group. Asset groups utilized in this analysis are identified as the lowest level grouping of assets for which largely independent cash flows can be identified. If impairment is indicated, the asset or asset group is written down to its estimated fair value.

Significant judgments and estimates are involved in determining the useful lives of our long-lived assets, determining the reporting units and assessing when events or circumstances would require an interim impairment analysis of goodwill or other long-lived assets to be performed. Changes in our organization or management reporting structure, as well as other events and circumstances, including but not limited to technological advances, increased competition and changing economic or market conditions, could result in (a) shorter estimated useful lives, (b) changes to reporting units, which may require alternative methods of estimating fair values or greater disaggregation or aggregation in our analysis by reporting unit, and/or (c) other changes in previous assumptions or estimates. In turn,

this could have a significant impact on our consolidated financial statements through accelerated amortization and/or impairment charges.

Accounting for Stock-Based Compensation. We account for share-based awards to employees and directors, including grants of employee stock options, purchases under employee stock purchase plans, awards in the form of restricted shares (“Restricted Stock”) and awards in the form of units of stock purchase rights (“Restricted Units”) through recognition of the fair value of the share-based awards as a charge against earnings in the form of stock-based compensation expense. We recognize stock-based compensation expense over the requisite service period, net of estimated forfeitures. We will recognize a benefit from stock-based compensation in equity using the with-and-without approach for the utilization of tax attributes. The Restricted Stock and Restricted Units are collectively referred to as “Restricted Awards.” Determining the fair value of share-based awards at the grant date requires judgment, including estimating expected dividends, share price volatility and the amount of share-based awards that are expected to be forfeited. If actual results differ significantly from these estimates, stock-based compensation expense and our results of operations could be materially impacted.

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Income Taxes. Deferred tax assets and liabilities are determined based on differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. We do not provide for U.S. income taxes on the undistributed earnings of our foreign subsidiaries, which we consider to be indefinitely reinvested outside of the U.S.

We make judgments regarding the realizability of our deferred tax assets. The balance sheet carrying value of our net deferred tax assets is based on whether we believe that it is more likely than not that we will generate sufficient future taxable income to realize these deferred tax assets after consideration of all available evidence. We regularly review our deferred tax assets for recoverability considering historical profitability, projected future taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies. In assessing the need for a valuation allowance, we consider both positive and negative evidence related to the likelihood of realization of the deferred tax assets. The weight given to the positive and negative evidence is commensurate with the extent to which the evidence may be objectively verified. As such, it is generally difficult for positive evidence regarding projected future taxable income exclusive of reversing taxable temporary differences to outweigh objective negative evidence of recent financial reporting losses. Generally, cumulative loss in recent years is a significant piece of negative evidence that is difficult to overcome in determining that a valuation allowance is not needed.

Through fiscal 2011, valuation allowances were established for certain deferred tax assets, which we believe did not meet the “more likely than not” criteria for recognition. At September 30, 2011, our valuation allowance was \$274.8 million. Prior to year end 2012, the pattern of objectively measured negative evidence of recent financial reporting losses outweighed the positive evidence of our profitability. By the end of fiscal 2012, our U.S. operations had pre-tax income adjusted for permanent differences in items of income and expense for the most recent three-year period. We concluded that this record of cumulative profitability in recent years and our business plan showing continued profitability provided assurance that our future tax benefits more likely than not will be realized. Accordingly, by the end of fiscal 2012, we made a determination that it is more likely than not that certain of our deferred taxes, primarily in the U.S., will be realized which resulted in a release of \$70.5 million of our valuation allowance (See Note 20 of Notes to our Consolidated Financial Statements).

As of September 30, 2012, we have \$89.4 million of valuation allowances remaining for certain foreign deferred tax assets. If we are subsequently able to utilize all or a portion of the deferred tax assets for which the remaining valuation allowance has been established, then we may be required to recognize these deferred tax assets through the reduction of the valuation allowance which could result in a material benefit to our results of operations in the period in which the benefit is determined.

We establish reserves for tax uncertainties that reflect the use of the comprehensive model for the recognition and measurement of uncertain tax positions. Under the comprehensive model, when the minimum threshold for recognition is not met, no tax benefit can be recorded. When the minimum threshold for recognition is met, a tax position is recorded as the largest amount that is more than fifty percent likely of being realized upon ultimate settlement.

Loss Contingencies. We are subject to legal proceedings, lawsuits and other claims relating to labor, service and other matters arising in the ordinary course of business, as discussed in Note 18 of Notes to our Consolidated Financial Statements. Quarterly, we review the status of each significant matter and assess our potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount can be reasonably estimated, we accrue a liability for the estimated loss. Significant judgment is required in both the determination of probability and the determination as to whether an exposure is reasonably estimable. Because of uncertainties related to these matters, accruals are based only on the best information available at the time. As additional information becomes available, we reassess the potential liability related to our pending claims and litigation and may revise our estimates. Such revisions in the estimates of the potential liabilities could have a material impact on our results of

operations and financial position.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In July 2012, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2012-02, Intangibles-Goodwill and Other (Topic 350)-Testing Indefinite-Lived Intangible Assets for Impairment ("ASU 2012-02"), to allow entities to use a qualitative approach to test indefinite-lived intangible assets for impairment. ASU 2012-02 permits an entity to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the currently prescribed quantitative impairment test by comparing the fair value of the indefinite-lived intangible asset with its carrying value. Otherwise, the quantitative impairment test is not required. ASU 2012-02 is effective for fiscal years beginning after September 15, 2012. As we do not have any indefinite lived intangible assets other than goodwill, we do not expect this update to have a significant impact on our financial statements.

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Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risk from changes in foreign currency exchange rates, interest rates and equity prices which could affect operating results, financial position and cash flows. We manage our exposure to these market risks through our regular operating and financing activities and, when appropriate, through the use of derivative financial instruments.

Exchange Rate Sensitivity

We are exposed to changes in foreign currency exchange rates. Any foreign currency transaction, defined as a transaction denominated in a currency other than the U.S. dollar, will be reported in U.S. dollars at the applicable exchange rate. Assets and liabilities are translated into U.S. dollars at exchange rates in effect at the balance sheet date and income and expense items are translated at average rates for the period. The primary foreign currency denominated transactions include revenue and expenses and the resulting accounts receivable and accounts payable balances reflected on our balance sheet. Therefore, the change in the value of the U.S. dollar compared to foreign currencies will have either a positive or negative effect on our financial position and results of operations. Historically, our primary exposure has related to transactions denominated in the euro, British pound, Canadian dollar, Japanese yen, Indian rupee and Hungarian forint.

A hypothetical change of 10% in appreciation or depreciation in foreign currency exchange rates from the quoted foreign currency exchange rates at September 30, 2012 would not have a material impact on our revenue, operating results or cash flows in the coming year.

Periodically, we enter into forward exchange contracts to hedge against foreign currency fluctuations. These contracts may or may not be designated as cash flow hedges for accounting purposes. We have in place a program which primarily uses forward contracts to offset the risks associated with foreign currency exposures that arise from transactions denominated in currencies other than the functional currencies of our worldwide operations. The program is designed so that increases or decreases in our foreign currency exposures are offset by gain or losses on the foreign currency forward contracts. These contracts are not designated as accounting hedges and generally are for periods less than 90 days. The notional contract amount of outstanding foreign currency exchange contracts not designated as cash flow hedges was \$83.9 million at September 30, 2012. Based on the nature of the transactions for which the contracts were purchased, a hypothetical change of 10% in exchange rates would not have a material impact on our financial results.

Interest Rate Sensitivity

We are exposed to interest rate risk as a result of our significant cash and cash equivalents, and the outstanding debt under the Credit Facility.

At September 30, 2012, we held approximately \$1,129.8 million of cash and cash equivalents primarily consisting of cash and money-market funds. Due to the low current market yields and the short-term nature of our investments, a hypothetical change in market rates of one percentage point would not have a material effect on the fair value of our portfolio. Assuming a one percentage point increase in interest rates, our interest income on our cash and cash equivalents would increase approximately \$10.1 million, based on the September 30, 2012 reported balances of our investment accounts.

At September 30, 2012, our total outstanding debt balance exposed to variable interest rates was \$630.6 million. A hypothetical change in market rates would have a significant impact on interest expense and amounts payable. Assuming a one percentage point increase in interest rates, our interest expense relative to our outstanding variable

rate debt would increase \$6.4 million per annum.

Equity Price Risk

We are exposed to equity price risk as a result of security price guarantees that we enter in to from time to time. Generally, these price guarantees are for a period of six months or less, and require payment from either us to a third party, or from the third party to us, based upon changes in our stock price during the contract term. As of September 30, 2012, we have security price guarantees outstanding for approximately 1.0 million shares of our common stock. A 10% change in our stock price during the next six months would not have a material impact on our statements of operations or cash flows.

2027 and 2031 Debentures

The fair value of our 2031 and 2027 Debentures is dependent on the price and volatility of our common stock as well as movements in interest rates. The fair market value of the debentures will generally increase or decrease as the market price of our

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common stock changes. The fair market value of the debentures will generally increase as interest rates fall and decrease as interest rates rise. The market value and interest rate changes affect the fair market value of the debentures, but do not impact our financial position, cash flows or results of operations due to the fixed nature of the debt obligations. However, increases in the value of our common stock above the stated trigger price for each issuance for a specified period of time may provide the holders of the debentures the right to convert each bond using a conversion ratio and payment method as defined in the debenture agreement.

Our debentures trade in the financial markets, and the fair value at September 30, 2012 was \$800.1 million for the 2031 Debentures and \$359.0 million for the 2027 Debentures, based on an average of the bid and ask prices for each of the issuances on that day. This compares to conversion values on September 30, 2012 of approximately \$531.7 million and \$319.6 million for the 2031 Debentures and the 2027 Debentures, respectively. A 10% increase in the stock price over the September 30, 2012 closing price of \$24.89 would have an combined estimated \$63.3 million increase to the fair value and a combined \$85.1 million increase to the conversion value of the debentures. Given the current trading value of the debentures, the greatest value to the holders of the debentures would be to sell the debentures in the open market in order to maximize their return. Based on this, we believe that the holders may not have a significant economic incentive to convert prior to the first redemption date.

Item 8. Financial Statements and Supplementary Data

Nuance Communications, Inc. Consolidated Financial Statements

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NUANCE COMMUNICATIONS, INC.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Nuance Communications, Inc.

Burlington, Massachusetts

We have audited the accompanying consolidated balance sheets of Nuance Communications, Inc. as of September 30, 2012 and 2011, and the related consolidated statements of operations, comprehensive income (loss), stockholders' equity, and cash flows for each of the three years in the period ended September 30, 2012. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Nuance Communications, Inc. at September 30, 2012 and 2011, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 2012, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Nuance Communications, Inc.'s internal control over financial reporting as of September 30, 2012, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations (COSO), and our report dated November 28, 2012 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP
BDO USA, LLP

Boston, Massachusetts

November 28, 2012

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Nuance Communications, Inc.
Burlington, Massachusetts

We have audited Nuance Communications, Inc.'s internal control over financial reporting as of September 30, 2012, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Nuance Communications, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Item 9A, Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, Nuance Communications, Inc. maintained, in all material respects, effective internal control over financial reporting as of September 30, 2012, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Nuance Communications, Inc. as of September 30, 2012 and 2011, and the related consolidated statements of operations, comprehensive income (loss), stockholders' equity and cash flows for each of the three years in the period ended September 30, 2012 and our report dated November 28, 2012 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP
BDO USA, LLP

Boston, Massachusetts
November 28, 2012

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NUANCE COMMUNICATIONS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended September 30,		
	2012	2011	2010
	(In thousands, except per share amounts)		
Revenues:			
Product and licensing	\$740,726	\$607,358	\$473,460
Professional services and hosting	673,943	509,141	463,567
Maintenance and support	236,840	202,242	181,921
Total revenues	1,651,509	1,318,741	1,118,948
Cost of revenues:			
Product and licensing	74,837	65,601	49,618
Professional services and hosting	424,733	341,055	280,725
Maintenance and support	45,325	38,057	31,269
Amortization of intangible assets	60,034	55,111	47,758
Total cost of revenues	604,929	499,824	409,370
Gross profit	1,046,580	818,917	709,578
Operating expenses:			
Research and development	225,441	179,377	152,071
Sales and marketing	369,205	306,439	266,208
General and administrative	163,318	147,603	122,061
Amortization of intangible assets	95,416	88,219	87,819
Acquisition-related costs, net	58,746	21,866	30,611
Restructuring and other charges, net	8,268	22,862	17,891
Total operating expenses	920,394	766,366	676,661
Income from operations	126,186	52,551	32,917
Other income (expense):			
Interest income	2,234	3,159	1,238
Interest expense	(85,286)	(36,703)	(40,993)
Other income, net	22,168	11,010	5,773
Income (loss) before income taxes	65,302	30,017	(1,065)
(Benefit) provision for income taxes	(141,833)	(8,221)	18,034
Net income (loss)	\$207,135	\$38,238	\$(19,099)
Net income (loss) per share:			
Basic	\$0.67	\$0.13	\$(0.07)
Diluted	\$0.65	\$0.12	\$(0.07)
Weighted average common shares outstanding:			
Basic	306,371	302,277	287,412
Diluted	320,822	315,960	287,412

See accompanying notes.

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NUANCE COMMUNICATIONS, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Year Ended September 30,		
	2012	2011	2010
	(In thousands)		
Net income (loss)	\$207,135	\$38,238	\$(19,099)
Other comprehensive income (loss):			
Unrealized (losses) gains on cash flow hedge derivatives	(20)	(210)	4,208
Unrealized gains (losses) on marketable securities	12	(42)	30
Foreign currency translation adjustment	(7,776)	(8,746)	(2,807)
Unrealized (losses) gains on pensions	(1,648)	2,895	(493)
Total other comprehensive (loss) income, net	(9,432)	(6,103)	938
Comprehensive income (loss)	\$197,703	\$32,135	\$(18,161)

See accompanying notes.

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NUANCE COMMUNICATIONS, INC.

CONSOLIDATED BALANCE SHEETS

	September 30, 2012	September 30, 2011
	(In thousands, except per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$1,129,761	\$447,224
Restricted cash (Note 9)	—	6,799
Marketable securities	—	31,244
Accounts receivable, less allowances for doubtful accounts of \$6,933 and \$5,707	381,417	280,856
Prepaid expenses and other current assets	102,564	88,804
Deferred tax asset	87,564	—
Total current assets	1,701,306	854,927
Land, building and equipment, net	116,134	78,218
Goodwill	2,955,477	2,347,880
Intangible assets, net	906,538	731,577
Other assets	119,585	82,691
Total assets	\$5,799,040	\$4,095,293
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	\$148,542	\$6,905
Redeemable convertible debentures	231,552	—
Contingent and deferred acquisition payments	49,685	23,783
Accounts payable	113,196	82,703
Accrued expenses and other current liabilities	215,178	176,074
Deferred revenue	206,610	185,605
Total current liabilities	964,763	475,070
Long-term portion of debt	1,735,811	853,020
Deferred revenue, net of current portion	108,481	90,382
Deferred tax liability	160,614	72,229
Other liabilities	82,665	111,221
Total liabilities	3,052,334	1,601,922
Commitments and contingencies (Notes 3, 5, and 18)		
Equity component of currently redeemable convertible debentures (Note 10)	18,430	—
Stockholders' equity:		
Series B preferred stock, \$0.001 par value; 15,000 shares authorized; 3,562 shares issued and outstanding (liquidation preference \$4,631)	4,631	4,631
Common stock, \$0.001 par value; 560,000 shares authorized; 315,821 and 312,456 shares issued and 312,070 and 308,705 shares outstanding	316	312
Additional paid-in capital	2,908,302	2,745,931
Treasury stock, at cost (3,751 and 3,751 shares)	(16,788	) (16,788
Accumulated other comprehensive (loss) income	(7,030	) 2,402
Accumulated deficit	(161,155	) (243,117
Total stockholders' equity	2,728,276	2,493,371
Total liabilities and stockholders' equity	\$5,799,040	\$4,095,293
See accompanying notes.		

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 NUANCE COMMUNICATIONS, INC.
 CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Preferred Stock		Common Stock			Additional Paid-In Capital		Treasury Stock		Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount	Shares	Amount	Capital	Shares	Amount					
	(In thousands)											
Balance at October 1, 2009	3,562	4,631	280,647	281	2,308,992	3,712	(16,214)	7,567	(262,256)		2,043,001	
Issuance of common stock under employee stock plans			10,139	10	29,500						29,510	
Cancellation of restricted stock, and repurchase of common stock at cost for employee tax withholding			(1,635)	(2)	(25,973)	(39)	(574)				(26,549)	
Stock-based compensation					100,139						100,139	
Excess tax benefit from share-based payment plans					1,060						1,060	
Issuance of common stock in connection with warrant exercises			2,509	3	12,347						12,350	
Issuance of common stock in connection with business and asset acquisitions			6,845	7	106,329						106,336	
Issuance of common stock in connection with collaboration agreements			2,524	2	39,298						39,300	
Payments for escrow, make-whole and earn-out settlements			594	1	10,209						10,210	

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Net loss									(19,099)	(19,099)
Other comprehensive income								938		938
Balance at September 30, 2010	3,562	4,631	301,623	302	2,581,901	3,673	(16,788)	8,505	(281,355)	2,297,196
Issuance of common stock under employee stock plans			11,052	11	36,656					36,667
Cancellation of restricted stock, and repurchase of common stock at cost for employee tax withholding			(1,996)	(2)	(36,705)	78	—			(36,707)
Stock-based compensation					112,469					112,469
Excess tax benefit from share-based payment plans					17,520					17,520
Issuance of common stock in connection with business and asset acquisitions			486	—	10,000					10,000
Issuance of common stock in connection with collaboration agreements			1,274	1	23,399					23,400
Payments for escrow, make-whole and earn-out settlements			17	—	691					691
Net income									38,238	38,238
Other comprehensive loss								(6,103)		(6,103)
Balance at September 30, 2011	3,562	4,631	312,456	312	2,745,931	3,751	(16,788)	2,402	(243,117)	2,493,371
Issuance of common stock under employee			9,891	10	27,737					27,747

stock plans										
Cancellation of restricted stock, and repurchase of common stock at cost for employee tax withholding	(2,158)	(2)	(52,000)						(52,002)	
Stock-based compensation			161,165						161,165	
Excess tax benefit from share-based payment plans			(3,583)						(3,583)	
Repurchase of common stock	(8,514)	(8)	(74,816)					(125,173)	(199,997)	
Equity portion of convertible debt issuance, net of tax effect			96,934						96,934	
Issuance of common stock in connection with collaboration agreements	1,010	1	23,399						23,400	
Payments for escrow, make-whole and earn-out settlements	60	—	1,968						1,968	
Issuance of common stock in connection with warrant exercises	3,076	3	(3)						—	
Reclassification to temporary equity			(18,430)						(18,430)	
Net income								207,135	207,135	
Other comprehensive loss								(9,432)	(9,432)	
Balance at September 30, 2012	3,562	\$4,631	315,821	\$316	\$2,908,302	3,751	\$(16,788)	\$(7,030)	\$(161,155)	\$2,728,276

See accompanying notes.

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NUANCE COMMUNICATIONS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended September 30,		
	2012	2011	2010
	(In thousands)		
Cash flows from operating activities			
Net income (loss)	\$207,135	\$38,238	\$(19,099)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	187,183	170,933	157,156
Stock-based compensation	174,581	147,296	100,139
Non-cash interest expense	35,497	12,510	12,955
Non-cash restructuring expense	—	11,725	6,833
Deferred tax (benefit) provision	(151,547)	(43,890)	3,742
Gain on non-controlling strategic equity interest	(13,726)	—	—
Other	4,016	16,492	1,576
Changes in operating assets and liabilities, net of effects from acquisitions:			
Accounts receivable	(55,210)	(25,530)	(773)
Prepaid expenses and other assets	13,881	(11,793)	(3,840)
Accounts payable	22,645	(8,193)	4,710
Accrued expenses and other liabilities	8,939	(6,775)	(6,760)
Deferred revenue	39,605	56,398	39,643
Net cash provided by operating activities	472,999	357,411	296,282
Cash flows from investing activities			
Capital expenditures	(62,910)	(34,907)	(25,974)
Payments for business and technology acquisitions, net of cash acquired	(884,945)	(409,005)	(219,029)
Purchases of marketable securities and other investments	(15,156)	(10,776)	(48,499)
Proceeds from sales and maturities of marketable securities and other investments	31,789	11,650	—
Change in restricted cash balances	6,747	17,184	(22,070)
Net cash used in investing activities	(924,475)	(425,854)	(315,572)
Cash flows from financing activities			
Payments of long-term debt	(6,605)	(7,535)	(8,460)
Proceeds from long-term debt, net of issuance costs	1,364,925	(2,553)	—
Payments for repurchase of common stock	(199,997)	—	—
Proceeds from issuance of common stock, net of issuance costs	—	—	12,350
Payments on other long-term liabilities	(8,525)	(10,643)	(9,870)
Proceeds from settlement of share-based derivatives, net	9,020	9,414	7,306
Excess tax benefits on employee equity awards	(3,583)	17,520	1,060
Proceeds from issuance of common stock from employee stock plans	27,747	36,667	29,510
Cash used to net share settle employee equity awards	(49,947)	(36,908)	(22,016)
Net cash provided by financing activities	1,133,035	5,962	9,880
Effects of exchange rate changes on cash and cash equivalents	978	(6,925)	(998)
Net increase (decrease) in cash and cash equivalents	682,537	(69,406)	(10,408)
Cash and cash equivalents at beginning of year	447,224	516,630	527,038

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Cash and cash equivalents at end of year	\$1,129,761	\$447,224	\$516,630
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See accompanying notes.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Presentation

Nuance Communications, Inc. (“we,” “Nuance,” or “the Company”) is a leading provider of voice and language solutions for businesses and consumers around the world. Our technologies, applications and services make the user experience more compelling by transforming the way people interact with devices and systems. Our solutions are used for tasks and services such as requesting information from a phone-based self-service solution, dictating medical records, searching the mobile Web by voice, entering a destination into a navigation system, or working with PDF documents. Our solutions help make these interactions, tasks and experiences more productive, compelling and efficient.

We leverage our global professional services organization and our extensive network of partners to design and deploy innovative solutions for businesses and organizations around the globe. We market and sell our products directly through a dedicated sales force, our e-commerce website and a global network of resellers, including system integrators, independent software vendors, value-added resellers, hardware vendors, telecommunications carriers and distributors.

We have built a portfolio of intellectual property, technologies, applications and solutions through both internal development and acquisitions. We expect to continue to pursue opportunities to expand our assets, geographic presence, distribution network and customer base through acquisitions of other businesses and technologies. Significant business acquisitions during fiscal 2012, 2011 and 2010 were as follows:

- ¶ June 1, 2012 — Vlingo Corporation ("Vlingo")
- ¶ April 26, 2012 — Transcend Services, Inc. ("Transcend")
- ¶ June 16, 2011 — SVOX, A.G. ("SVOX")
- ¶ June 15, 2011 — Equitrac Corporation ("Equitrac")
- ¶ December 30, 2009 — SpinVox, Limited ("SpinVox")

The results of operations from the acquired businesses have been included in our consolidated financial statements from their respective acquisition dates. See Note 3 for additional disclosure related to each of these acquisitions.

We operate in four reportable segments; Healthcare, Mobile and Consumer, Enterprise, and Imaging. See Note 22 for a description of each of these segments.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. On an ongoing basis, we evaluate our estimates, assumptions and judgments. The most important of these relate to revenue recognition; the allowances for doubtful accounts and sales returns; the valuation of goodwill and intangible assets; accounting for business combinations; accounting for stock-based compensation; the accounting for derivative instruments; accounting for income taxes and related valuation allowances; and loss contingencies. We base our estimates on historical experience, market participant fair value considerations and various other factors that are believed to be reasonable under the circumstances. Actual

amounts could differ significantly from these estimates.

Basis of Consolidation

The consolidated financial statements include our accounts and those of our wholly-owned domestic and foreign subsidiaries. Intercompany transactions and balances have been eliminated.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Reclassification

We reclassified certain items included within the balance sheet as of September 30, 2011 to conform with the current year presentation. The reclassification includes combining acquired unbilled accounts receivable with accounts receivable. Such reclassifications have no impact on earnings or cash flows provided by operations.

Revenue Recognition

We derive revenue from the following sources: (1) software license agreements, including royalty and other usage-based arrangements, (2) professional services, (3) hosting services and (4) post-contract customer support ("PCS"). Our hosting services are generally provided through on-demand, usage-based or per transaction fee arrangements. Our revenue recognition policies for these revenue streams are discussed below.

The sale and/or license of software products and technology is deemed to have occurred when a customer either has taken possession of or has access to take immediate possession of the software or technology. In select situations, we sell or license intellectual property in conjunction with, or in place of, embedding our intellectual property in software. We also have non-software arrangements including hosting services where the customer does not take possession of the software at the outset of the arrangement either because they have no contractual right to do so or because significant penalties preclude them from doing so. Generally we recognize revenue when (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable and (iv) collectibility is probable.

Revenue from royalties on sales of our software products by original equipment manufacturers ("OEMs"), where no services are included, is recognized in the quarter earned so long as we have been notified by the OEM that such royalties are due, and provided that all other revenue recognition criteria are met.

Software arrangements generally include PCS, which includes telephone support and the right to receive unspecified upgrades/enhancements on a when-and-if-available basis, typically for one to five years. Revenue from PCS is generally recognized ratably on a straight-line basis over the term that the maintenance service is provided. When PCS renews automatically, we provide a reserve based on historical experience for contracts expected to be canceled for non-payment. All known and estimated cancellations are recorded as a reduction to revenue and accounts receivable.

For our software and software-related multiple element arrangements, where customers purchase both software related products and software related services, we use vendor-specific objective evidence ("VSOE") of fair value for software and software-related services to separate the elements and account for them separately. VSOE exists when a company can support what the fair value of its software and/or software-related services is based on evidence of the prices charged when the same elements are sold separately. VSOE of fair value is required, generally, in order to separate the accounting for various elements in a software and related services arrangement. We have established VSOE of fair value for the majority of our PCS, professional services, and training.

When we provide professional services considered essential to the functionality of the software, we recognize revenue from the professional services as well as any related software licenses on a percentage-of-completion basis whereby the arrangement consideration is recognized as the services are performed, as measured by an observable input. In

these circumstances, we separate license revenue from professional service revenue for income statement presentation by allocating VSOE of fair value of the professional services as professional services and hosting revenue and the residual portion as product and licensing revenue. We generally determine the percentage-of-completion by comparing the labor hours incurred to-date to the estimated total labor hours required to complete the project. We consider labor hours to be the most reliable, available measure of progress on these projects. Adjustments to estimates to complete are made in the periods in which facts resulting in a change become known. When the estimate indicates that a loss will be incurred, such loss is recorded in the period identified. Significant judgments and estimates are involved in determining the percent complete of each contract. Different assumptions could yield materially different results.

We offer some of our products via a Software-as-a-Service ("SaaS") model also known as a hosted model. In this type of arrangement, we are compensated in two ways: (1) fees for up-front set-up of the service environment and (2) fees charged on a usage or per transaction basis. Our up-front set-up fees are nonrefundable. We recognize the up-front set-up fees ratably over the longer of the contract lives, or the expected lives of the customer relationships. The on-demand, usage-based or per transaction fees are due and payable as each individual transaction is processed through the hosted service and is recognized as revenue in the period the services are provided.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

We enter into multiple-element arrangements that may include a combination of our various software related and non-software related products and services offerings including software licenses, PCS, professional services, and our hosting services. In such arrangements we allocate total arrangement consideration to software or software-related elements and any non-software element separately based on the selling price hierarchy group following the guidance in ASC 985-605 and our policies. We determine the selling price for each deliverable using VSOE of selling price, if it exists, or Third Party Evidence (“TPE”) of selling price. Typically, we are unable to determine TPE of selling price. Therefore, when neither VSOE nor TPE of selling price exist for a deliverable, we use our Estimate of Selling Price (“ESP”) for the purposes of allocating the arrangement consideration. We determine ESP for a product or service by considering multiple factors including, but not limited to, major project groupings, market conditions, competitive landscape, price list and discounting practices. Revenue allocated to each element is then recognized when the basic revenue recognition criteria are met for each element.

When products are sold through distributors or resellers, title and risk of loss generally passes upon shipment, at which time the transaction is invoiced and payment is due. Shipments to distributors and resellers without right of return are recognized as revenue upon shipment, provided all other revenue recognition criteria are met. Certain distributors and resellers have been granted rights of return for as long as the distributors or resellers hold the inventory. We cannot use historical returns from these distributors and resellers as a basis upon which to estimate future sales returns. As a result, we recognize revenue from sales to these distributors and resellers when the products are sold through to retailers and end-users.

When products are sold directly to retailers or end-users, we make an estimate of sales returns based on historical experience. The provision for these estimated returns is recorded as a reduction of revenue and accounts receivable at the time that the related revenue is recorded. If actual returns differ significantly from our estimates, such differences could have a material impact on our results of operations for the period in which the actual returns become known.

We record consideration given to a reseller as a reduction of revenue to the extent we have recorded cumulative revenue from the customer or reseller. However, when we receive an identifiable benefit in exchange for the consideration, and can reasonably estimate the fair value of the benefit received, the consideration is recorded as an operating expense.

We record reimbursements received for out-of-pocket expenses as revenue, with offsetting costs recorded as cost of revenue. Out-of-pocket expenses generally include, but are not limited to, expenses related to transportation, lodging and meals. We record shipping and handling costs billed to customers as revenue with offsetting costs recorded as cost of revenue.

Deferred revenue at September 30, 2012 and 2011 were as follows (dollars in thousands):

	September 30, 2012	September 30, 2011
Current Liabilities:		
Deferred maintenance revenue	\$ 114,036	\$ 101,480
Unearned revenue	92,574	84,125

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Total current deferred revenue	\$206,610	\$185,605
Long-term Liabilities:		
Deferred maintenance revenue	\$43,763	\$22,712
Unearned revenue	64,718	67,670
Total long-term deferred revenue	\$108,481	\$90,382

Business Combinations

We determine and allocate the purchase price of an acquired company to the tangible and intangible assets acquired and liabilities assumed as of the business combination date. Results of operations and cash flows of acquired companies are included in our operating results from the date of acquisition. The purchase price allocation process requires us to use significant estimates and assumptions, including fair value estimates, as of the business combination date including:

- estimated fair values of intangible assets;
- estimated fair market values of legal performance commitments to customers, assumed from the acquiree under existing contractual obligations (classified as deferred revenue);

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

- estimated fair market values of stock awards assumed from the acquiree that are included in the purchase price;
- estimated fair market value of required payments under contingent consideration provisions;
- estimated income tax assets and liabilities assumed from the acquiree; and
- estimated fair value of pre-acquisition contingencies assumed from the acquiree.

While we use our best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the business combination date, our estimates and assumptions are inherently uncertain and subject to refinement. As a result, during the purchase price allocation period, which is generally one year from the business combination date, we record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. For changes in the valuation of intangible assets between preliminary and final purchase price allocation, the related amortization is adjusted effective from the acquisition date. Subsequent to the purchase price allocation period any adjustment to assets acquired or liabilities assumed is included in operating results in the period in which the adjustment is determined.

Goodwill and Indefinite-Lived Intangible Assets

Goodwill represents the excess of the purchase price in a business combination over the fair value of net tangible and intangible assets acquired. Goodwill and intangible assets with indefinite lives are not amortized, but rather the carrying amounts of these assets are reviewed for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value of these assets may not be recoverable. Our annual impairment assessment date is July 1 of each fiscal year. Goodwill is evaluated for impairment based on a comparison of the fair value of our reporting units to their recorded carrying values. We have seven reporting units based on the level of information provided to, and review thereof, by our segment management.

We determine fair values for each of the reporting units using an income approach. When available and appropriate, we also use a comparative market approach to derive the fair values. For purposes of the income approach, fair value is determined based on the present value of estimated future cash flows, discounted at an appropriate risk adjusted rate. We use our internal forecasts to estimate future cash flows and include an estimate of long-term future growth rates based on our most recent views of the long-term outlook for each business. Actual results may differ from those assumed in our forecasts. We derive our discount rates using a capital asset pricing model and analyzing published rates for industries relevant to our reporting units to estimate the cost of equity financing. We use discount rates that are commensurate with the risks and uncertainty inherent in the respective businesses and in our internally developed forecasts. Discount rates used in our reporting unit valuations ranged from 12% to 21%. For purposes of the market approach, we use a valuation technique in which values are derived based on market prices of comparable publicly traded companies. We also use a market based valuation technique in which values are determined based on relevant observable information generated by market transactions involving comparable businesses. We assess each valuation methodology based upon the relevance and availability of the data at the time we perform the valuation and weight the methodologies appropriately. The carrying values of the reporting units were determined based on an allocation of our assets and liabilities through specific allocation of certain assets and liabilities to the reporting units and an apportionment method based on relative size of the reporting units' revenues and operating expenses compared to the Company as a whole. Certain corporate assets that are not instrumental to the reporting units' operations and would not

be transferred to hypothetical purchasers of the reporting units were excluded from the reporting units' carrying values.

Long-Lived Assets

Our long-lived assets consist principally of acquired intangible assets and land, building and equipment. Land, building and equipment are stated at cost. Building and equipment are depreciated over their estimated useful lives. Leasehold improvements are depreciated over the shorter of the related lease term or the estimated useful life. Costs of significant improvements on existing software for internal use are capitalized and depreciated over the estimated useful life. Depreciation is computed using the straight-line method. Repair and maintenance costs are expensed as incurred. The cost and related accumulated depreciation of sold or retired assets are removed from the accounts and any gain or loss is included in operations.

We include in our amortizable intangible assets those intangible assets acquired in our business and asset acquisitions, including certain technology that is licensed from third parties. We amortize acquired intangible assets with finite lives over the estimated economic lives of the assets, generally using the straight-line method except where the pattern of the expected economic benefit is readily identifiable, primarily customer relationship intangibles, whereby amortization follows that pattern. Each period, we evaluate the estimated remaining useful life of acquired and licensed intangible assets, as well as land, buildings and equipment, to determine whether events or changes in circumstances warrant a revision to the remaining period of depreciation or amortization.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

We evaluate long-lived assets for impairment whenever events or changes in circumstances indicate the carrying value of an asset or asset group may not be recoverable. We assess the recoverability of the asset or asset group based on the undiscounted future cash flows the assets are expected to generate, and recognize an impairment loss when estimated undiscounted future cash flows expected to result from the use of the assets plus net proceeds expected from disposition of the assets, if any, are less than the carrying value of the assets. If an asset or asset group is deemed to be impaired, the amount of the impairment loss, if any, represents the excess of the asset or asset group's carrying value compared to its estimated fair value.

Cash and Cash Equivalents

Cash and cash equivalents consists of cash on hand, including money market funds and time deposits with original maturities of 90 days or less.

Marketable Securities and Minority Investments

Marketable Securities: Investments are classified as available-for-sale and are recorded on the balance sheet at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income, net of tax. Marketable securities consist primarily of high-quality corporate debt instruments. As of September 30, 2011, the total cost basis was \$31.3 million.

Minority Investment: We record investments in other companies, where we do not have a controlling interest or significant influence in the equity investment, at cost within other assets in our consolidated balance sheet. We review our investments for impairment whenever declines in estimated fair value are deemed to be other-than-temporary.

Accounts Receivable Allowances

Allowances for Doubtful Accounts: We maintain an allowance for doubtful accounts for the estimated probable losses on uncollectible accounts receivable. The allowance is based upon the credit worthiness of our customers, our historical experience, the age of the receivable and current market and economic conditions. Receivables are written off against these allowances in the period they are determined to be uncollectible.

Allowances for Sales Returns: We maintain an allowance for sales returns from customers for which we have the ability to estimate returns based on historical experience. The returns allowance is recorded as a reduction in revenue and accounts receivable at the time the related revenue is recorded. Receivables are written off against the allowance in the period the return is received.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

For the years ended September 30, 2012, 2011 and 2010, the activity related to accounts receivable allowances was as follows (dollars in thousands):

	Allowance for Doubtful Accounts	Allowance for Sales Returns
Balance at October 1, 2009	\$6,833	\$6,106
Bad debt provision	873	—
Write-offs, net of recoveries	(1,405))
Revenue adjustments, net	—	723
Balance at September 30, 2010	\$6,301	\$6,829
Bad debt provisions	1,332	—
Write-offs, net of recoveries	(1,926))
Revenue adjustments, net	—	(596)
Balance at September 30, 2011	\$5,707	\$6,233
Bad debt provisions	2,706	—
Write-offs, net of recoveries	(1,480))
Revenue adjustments, net	—	3,635
Balance at September 30, 2012	\$6,933	\$9,868

Inventories

Inventories are stated at the lower of cost, computed using the first-in, first-out method, or market value and are included in other current assets. We regularly review inventory quantities on hand and record a provision for excess and/or obsolete inventory primarily based on future purchase commitments with our suppliers, and the estimated utility of our inventory as well as other factors including technological changes and new product development.

Inventories, net of allowances, consisted of the following (dollars in thousands):

	September 30, 2012	September 30, 2011
Components and parts	\$7,562	\$6,279
Inventory at customers	—	275
Finished products	3,813	4,797
	\$11,375	\$11,351

Accounting for Collaboration Agreements

Healthcare Collaboration Agreement

In June 2011, we entered into an agreement with a large healthcare provider to acquire certain data for \$10.0 million, to be used in a joint development project. In addition, under the terms of the arrangement we will be reimbursed for certain research and development costs related to specified product development projects with the objective of commercializing the resulting products. All intellectual property derived from these research and development efforts

will be owned by us. Upon product introduction, we will pay royalties to this party based on the actual sales. At the end of five years, the party can elect to continue with the arrangement, receiving royalties on future sales, or receive a buy-out payment from us and forgo future royalties. The buy-out payment is calculated based on a number of factors including the net cash flows received and paid by the parties, as well as a minimum return on those net cash flows.

As of the execution of the above arrangement, we have other arrangements where we have sold and will continue to sell our products and services to this party. As a result, under the guidance of ASC 605, Revenue Recognition, we are required to reduce the revenue recognized by the amount we pay to this customer, up to our historical revenue recorded from them. We have therefore reduced reported revenue by \$10.0 million for the fiscal year ended September 30, 2011.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The above development arrangement will be accounted for in accordance with ASC 730, Research and Development. Accordingly, any buy-out obligation will be recorded as a liability and any reimbursement of the research and development costs in excess of the buy-out obligation will be recorded as an offset to research and development costs. Royalties paid to this party upon commercialization of any products from these development efforts will be recorded as a reduction to revenue in accordance with ASC 605. For fiscal year ended September 30, 2012 and September 30, 2011, \$5.8 million and \$5.9 million respectively of expense reimbursement has been recorded as a reduction in research and development expense.

Intellectual Property Collaboration Agreements

In order to gain access to a third party's extensive speech recognition technology, natural language and semantic process technology, in fiscal 2010 and 2011 we entered into three intellectual property collaboration agreements with terms up to six years. Generally, the agreements call for annual payments in cash or shares of our common stock, at our election. Payments are estimated to be \$23.4 million and \$5.0 million in each of the next two years. Depending on the agreement, some or all intellectual property derived from these collaborations will be jointly owned by the two parties. For the majority of the developed intellectual property, we will have sole rights to commercialize such intellectual property for periods ranging between two to six years, depending on the agreement. We issued 1.0 million and 1.3 million shares of our common stock for payments totaling \$23.4 million in each of the fiscal years ending in 2012 and 2011, respectively.

The payments are recorded as a prepaid asset when made, and will be expensed ratably over the contractual period. For the years ended September 30, 2012 and 2011, we have recognized \$21.0 million and \$19.8 million as research and development expense, respectively, related to these agreements in our consolidated statements of operations.

Research and Development Costs

Research and development costs related to software that is or will be sold or licensed externally to third-parties, or for which a substantive plan exists to sell or license such software in the future, incurred subsequent to the establishment of technological feasibility, but prior to the general release of the product, are capitalized and amortized to cost of revenue over the estimated useful life of the related products. We have determined that technological feasibility is reached shortly before the general release of our software products. Costs incurred after technological feasibility is established have not been material. We expense research and development costs as incurred.

Capitalized Patent Defense Costs

We monitor the anticipated outcome of legal actions, and if we determine that the success of the defense of a patent is probable, and so long as we believe that the future economic benefit of the patent will be increased, we capitalize external legal costs incurred in the defense of these patents, up to the level of the expected increased future economic benefit. If changes in the anticipated outcome occur, we write-off any capitalized costs in the period the change is determined. Upon successful defense of the patent, the amounts previously capitalized are amortized over the remaining life of the patent. During fiscal 2010, we expensed \$6.8 million of deferred costs included in restructuring and other charges, net, as a result of unsuccessful litigation. As of September 30, 2012 and 2011, there are no

capitalized patent defense costs.

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Acquisition-Related Costs, net

Acquisition-related costs include those costs related to business and other acquisitions, including potential acquisitions. These costs consist of (i) transition and integration costs, including retention payments, transitional employee costs and earn-out payments treated as compensation expense, as well as the costs of integration-related services provided by third-parties; (ii) professional service fees, including third-party costs related to the acquisitions, and legal and other professional service fees associated with disputes and regulatory matters related to acquired entities; and (iii) adjustments to acquisition-related items that are required to be marked to fair value each reporting period, such as contingent consideration, and other items related to acquisitions for which the measurement period has ended. The following is a summary of acquisition-related costs reported for the years ended September 30, 2012, 2011 and 2010, respectively (dollars in thousands):

	2012	2011	2010
Professional service fees	\$48,401	\$18,030	\$17,156
Transition and integration costs	9,888	3,361	13,562
Acquisition-related adjustments	457	475	(107)
Total	\$58,746	\$21,866	\$30,611

Advertising Costs

Advertising costs are expensed as incurred and are classified as sales and marketing expenses. Cooperative advertising programs reimburse customers for marketing activities for certain of our products, subject to defined criteria. Cooperative advertising obligations are accrued and the costs expensed at the same time the related revenue is recognized. Cooperative advertising expenses are recorded as expense to the extent that an advertising benefit separate from the revenue transaction can be identified and the cash paid does not exceed the fair value of that advertising benefit received. Any excess of cash paid over the fair value of the advertising benefit received is recorded as a reduction in revenue. We incurred advertising costs of \$40.5 million, \$30.6 million and \$21.1 million for fiscal 2012, 2011 and 2010, respectively.

Convertible Debt

We separately account for the liability (debt) and equity (conversion option) components of our convertible debt instruments that require or permit settlement in cash upon conversion in a manner that reflects our nonconvertible debt borrowing rate at the time of issuance. The equity components of our convertible debt instruments are recorded to stockholders' equity with an offsetting debt discount. The debt discount created is amortized to interest expense in our consolidated statement of operations using the effective interest method over the expected term of the convertible debt.

Income Taxes

Deferred tax assets and liabilities are determined based on differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. We do not provide for U.S. income taxes on the undistributed earnings of our foreign subsidiaries, which we consider to

be indefinitely reinvested outside of the U.S.

We make judgments regarding the realizability of our deferred tax assets. The balance sheet carrying value of our net deferred tax assets is based on whether we believe that it is more likely than not that we will generate sufficient future taxable income to realize these deferred tax assets after consideration of all available evidence. We regularly review our deferred tax assets for recoverability considering historical profitability, projected future taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies. In assessing the need for a valuation allowance, we consider both positive and negative evidence related to the likelihood of realization of the deferred tax assets. The weight given to the positive and negative evidence is commensurate with the extent to which the evidence may be objectively verified. As such, it is generally difficult for positive evidence regarding projected future taxable income exclusive of reversing taxable temporary differences to outweigh objective negative evidence of recent financial reporting losses. Generally, cumulative loss in recent years is a significant piece of negative evidence that is difficult to overcome in determining that a valuation allowance is not needed.

Valuation allowances have been established for certain foreign deferred tax assets, which we believe do not meet the “more likely than not” criteria for recognition. If we are subsequently able to utilize all or a portion of the deferred tax assets for which a valuation allowance has been established, then we may be required to recognize these deferred tax assets through the reduction

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NUANCE COMMUNICATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

of the valuation allowance which could result in a material benefit to our results of operations in the period in which the benefit is determined.

Comprehensive Income (Loss)

In June 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2011-05, Comprehensive Income: Presentation of Comprehensive Income. This ASU amends FASB Codification Topic 220, Comprehensive Income, to require an entity to present the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 is effective for fiscal years and interim periods within those fiscal years beginning after December 15, 2011 and early adoption is permitted. We adopted this ASU during the year ended September 30, 2012 and elected to present separate consolidated statements of comprehensive income (loss). In December 2011, the FASB issued ASC 2011-12 which amends ASU 2011-05 to defer only those changes in ASU 2011-05 that relate to the presentation of reclassification adjustments to allow the Board time to re-deliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. The adoption of this standard, will not have a significant impact on our financial statements.

For the purposes of comprehensive income (loss) disclosures, we do not record tax provisions or benefits for the net changes in the foreign currency translation adjustment, as we intend to reinvest undistributed earnings in our foreign subsidiaries permanently.

The components of accumulated other comprehensive (loss) income, reflected in the consolidated statements of stockholders' equity, consisted of the following (dollars in thousands):

	2012	2011	2010
Foreign currency translation adjustment	\$(3,456	) \$4,320	\$13,067
Unrealized (losses) gains on marketable securities	—	(12	) 30
Net unrealized gains on cash flow hedge derivatives	—	20	230
Net unrealized losses on post-retirement benefits	(3,574	) (1,926	) (4,822