OVERSEAS SHIPHOLDING GROUP INC
Form 10-K
February 29, 2012

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

FOR ANNUAL AND TRANSITION REPORTS

PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

(Mark One)

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

For the fiscal year ended December 31, 2011

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 1-6479-1

OVERSEAS SHIPHOLDING GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	13-2637623
(State or other jurisdiction of	(I.R.S. Employer
incorporation or organization)	Identification Number)
666 Third Avenue, New York, New York	10017
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code: 212-953-4100

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock (par value $1.00 per share)	New York Stock Exchange

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 x No ¨

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

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 x 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 definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

The aggregate market value of the Common Stock held by non-affiliates of the registrant on June 30, 2011, the last business day of the registrant's most recently completed second quarter, was $703,040,410, based on the closing price of $26.94 per share on the New York Stock Exchange on that date. (For this purpose, all outstanding shares of Common Stock have been considered held by non-affiliates, other than the shares beneficially owned by directors, officers and certain 5% shareholders of the registrant; certain of such persons disclaim that they are affiliates of the registrant.)

As of February 23, 2012, 30,446,257 shares of Common Stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be filed by the registrant in connection with its 2012 Annual Meeting of Shareholders are incorporated by reference in Part III.

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PART I

ITEM 1. BUSINESS

OVERVIEW

Overseas Shipholding Group, Inc. ("OSG" or the "Company") is one of the world's leading tanker companies engaged primarily in the ocean transportation of crude oil and petroleum products. At December 31, 2011, the Company owned or operated a modern fleet of 111 double-hulled vessels (aggregating 10.9 million deadweight tons and 864,800 cubic meters) of which 89 vessels operated in the international market and 22 operated in the U.S. Flag market. OSG's newbuilding program of owned and chartered-in vessels totaled five International Flag vessels, bringing the Company's total owned, operated and newbuild fleet to 116 double-hulled vessels. The Marshall Islands is the principal flag of registry of the Company's International Flag vessels. Additional information about the Company's fleet, including its ownership profile, is set forth below under Operations – Fleet Summary, as well as on the Company's website, www.osg.com.

The Company's vessel operations are organized into strategic business units and focused on broad market segments: crude oil, refined petroleum products, and U.S. Flag. The International Flag Crude Tanker unit manages International Flag ULCC, VLCC, Suezmax, Aframax, Panamax and Lightering tankers; the International Flag Product Carrier unit principally manages LR1 and MR product carriers and the U.S. unit manages the Company's U.S. Flag vessels. Through joint venture partnerships, the Company operates four LNG carriers and two Floating Storage and Offloading ("FSO") service vessels. Dedicated chartering and commercial personnel manage specific fleets while the Company's technical ship management operations and corporate departments support the Company's global operations.

OSG generally charters its vessels to customers either for specific voyages at spot rates or for specific periods of time at fixed daily amounts. Spot market rates are highly volatile; while time and bareboat charter rates, because they are fixed for specific periods of time, provide a more predictable stream of Time Charter Equivalent revenues ("TCE" revenues). For a more detailed discussion on factors influencing spot and time charter markets, see Operations—Charter Types later in this section.

A glossary of shipping terms (the "Glossary") that should be used as a reference when reading this Annual Report on Form 10-K can be found later in Item 1. Capitalized terms that are used in this Annual Report are either defined when they are first used or in the Glossary.

BUSINESS STRATEGY

OSG is committed to providing safe, reliable transportation services to its customers while ensuring the safety of its crews, vessels and the environment. The Company is also committed to creating long-term shareholder value by executing on a strategy designed to diversify its revenue sources across its chosen sectors and thereby maximize returns and reduce risk over shipping cycles. OSG's strategy is focused on four elements:

§ Sector Leadership

OSG seeks to maintain or achieve market leading positions in each of the primary markets it operates: crude oil, products and U.S. Flag. The Company has expanded its fleet through organic growth and acquisitions of companies that have expanded its market presence, the scale of its fleet and service offerings.

§ Fleet Optimization

The Company believes that it can improve returns in any shipping cycle by taking a portfolio approach to managing its business. This approach includes operating a diverse set of vessels that trade in different markets; participating in commercial pools that maximize vessel utilization; managing a fleet of owned and chartered-in tonnage that provides for flexibility and optionality; and trading its fleet in both the spot and time charter markets to enhance returns.

§ Superior Technical Ship Management

OSG is committed to operational excellence across its fleet. The Company's high-quality, modern fleet is operated by experienced crews supported by skilled shore side personnel. OSG's Safety Management System ("SMS") is designed to ensure that operational practices and procedures are standardized fleet wide and that seafarers and vessel operations meet or exceed all applicable safety, regulatory and environmental standards established by International and U.S. maritime laws. For more information, see Technical Operations later in this section.

§ Financial Flexibility

The Company believes its comparatively strong balance sheet, proven access to the capital markets and a significant unencumbered asset base provide financial flexibility. This financial flexibility assists the Company in navigating through the current weak industry conditions.

Summary of 2011 Events

OSG's strategy seeks to balance the expansion and renewal of its fleet across multiple market segments and manage the mix of owned and chartered-in assets. Chartering-in vessels gives the Company greater flexibility in both contracting and expanding markets through an ability to exercise redelivery, purchase or charter extension options. Sale and leaseback transactions not only raise cash that can be redeployed or reinvested, but shift risk, providing for greater flexibility in uncertain market conditions.

Fleet Expansion

In 2011, OSG took delivery of ten vessels.

§ In the Crude Oil segment, one 298,000 dwt owned VLCC, the Overseas McKinley, delivered in July.

§ In the Products segment, two LR1s, four MRs and one chemical tanker delivered. The LR1s included the Overseas Leyte and the Overseas Samar, both 74,000 dwt owned newbuilds that delivered in May and July, respectively. The MRs included the Overseas Milos, a 50,000 dwt owned newbuild, which delivered in August; the Atlantic Grace and the Atlantic Star, both 47,000 dwt that delivered in February and March, respectively, and the Freja Taurus, a 50,000 dwt newbuild that delivered in June. Three of the MRs were time chartered-in for three years. The Valorous Queen, a 19,900 dwt newbuild chemical tanker, time chartered-in for five years, delivered in September.

§ In the U.S. segment, the OSG Horizon/OSG 351, a 45,600 dwt owned lightering ATB, and the Overseas Tampa, a 46,815 dwt product carrier that is bareboat chartered-in for 10 years, delivered in April 2011.

Sale Transactions

During 2011, the Company sold its two remaining single-hulled U.S. Flag tankers, the Overseas Puget Sound and Overseas New Orleans, one chartered-in single-hull International Flag Aframax, the Brazos I, a chartered-in lightering vessel in which the Company had a residual value interest; an older owned lightering ATB, the OSG Constitution/OSG 400; and two tug boats. These transactions generated total proceeds of $19.6 million.

Managing Charter-in Portfolio

OSG continued to actively manage its Crude Oil segment charter-in portfolio this year by exercising restraint in extending or entering into new high cost long-term charter-in arrangements. Approximately twelve high cost charter-ins with redelivery dates heavily weighted to the first half of 2012 will either be returned or extended at lower rate levels. Five of these vessels were originally chartered in under sale leaseback arrangements that produced material capital gains. Being able to eliminate or

renegotiate favorable extensions on these loss making time charter-in arrangements is expected to yield better results for our chartered-in portfolio going forward.

During January 2011, the Crude Oil segment redelivered one bareboat chartered-in Aframax, the Overseas Jacamar, and one time chartered-in Aframax, the Aqua. The Company had less than 100% interest in the Aqua. Two VLCCs, the Overseas Meridian and the TI Watban, were also redelivered in June and August, respectively. In December 2011, OSG committed to a three-year time charter-in for a newbuild Suezmax that delivered in January 2012.

The Products segment redelivered one bareboat chartered-in LR2, the Overseas Takamar, and one time chartered-in MR, the Blue Emerald, in January and April, respectively.

Orderbook Amendments

In June 2011, OSG amended three newbuild order contracts, which resulted in, among other things:

- A delay of the delivery date of a newbuild MR to January 2012; and
- Contract price concessions on one newbuild MR that delivered in January 2012 and two Aframaxes scheduled for delivery in 2013.

Commercial Pools

To increase vessel utilization and thereby revenues, the Company participates in Commercial Pools with other like-minded shipowners of similar well-maintained vessels. By operating a large number of vessels as an integrated transportation system, Commercial Pools offer customers greater flexibility and a higher level of service while achieving scheduling efficiencies. Pools consist of experienced commercial operators, while technical management is performed by each shipowner. Pools negotiate charters with customers primarily in the spot market. The size and scope of these pools enable them to enhance utilization for pool vessels by securing backhaul voyages and Contracts of Affreightment ("COAs") and reduce waiting time, thus generating higher effective TCE revenues than otherwise might be obtainable in the spot market while providing a higher level of service to customers. As of December 31, 2011, OSG participates in five pools: Tankers International ("TI"), Aframax International ("AI"), Panamax International ("PI"), Clean Products International ("CPI") and Suezmax International ("SI"). For more information on the pools, see Operations—International Fleet Operations.

Technical Operations

OSG's global fleet operations are managed on an integrated basis by segment: crude, products and U.S. Flag. In addition to regular maintenance and repair, crews onboard each vessel and shore side personnel are responsible for ensuring that the Company's fleet meets or exceeds regulatory standards established by the International Maritime Organization ("IMO") and U.S. Coast Guard.

The Company is committed to providing safe, reliable and environmentally sound transportation to its customers. Integral to meeting standards mandated by worldwide regulators and customers is the Company's SMS. The SMS is a framework of processes and procedures that addresses a spectrum of operational risks associated with quality, environment, health and safety. The SMS is certified by ISM (International Safety Management Code), ISO 9001 (Quality Management) and ISO 14001 (Environmental Management).

The Company recruits, hires and trains the crews on its vessels. OSG's mandatory training and education requirements exceed the IMO Standards of Training, Certification and Watchkeeping (STCW). In early 2009, OSG completed the installation of an integrated engine room and bridge simulator located in its Manila office. In 2010, a cargo handling simulator was added. These simulators are used to familiarize OSG engine and deck officers with correct procedures and to train for unusual or unexpected situations. OSG believes its ability to provide professional development and long-term employment opportunities for qualified crew are competitive advantages in a market where skilled labor shortages are expected to remain a challenge. In 2011, both International and U.S. Flag crew retention was greater than 95%.

The fleet is supported by shore side operations that include fleet managers, marine and technical superintendents, purchasing staff, security officers, crewing and training personnel and a safety, quality and environmental ("SQE") department. Further augmenting technical operations are assurance functions that conduct vessel audits and assure compliance with marine and environmental regulations and manage preparedness for emergency response. OSG has an open reporting system whereby seafarers can anonymously report possible violations of Company policies and procedures. All open reports are investigated and appropriate actions are taken as needed. Furthermore, the Company's Vice President, Marine Operations Assurance and Response has independent oversight of fleet-wide vessel operating practices and procedures and global training programs.

Commercial Teams

OSG's commercial teams based in offices in Houston, London, Montreal, New York, Singapore, Newark (Delaware) and Tampa enable customers to have access, at all times, to information about their cargo's position and status. The Company believes that the scale of its fleet, its commercial management skills and its extensive market knowledge allow it to achieve better rates than smaller shipowners on a consistent basis. OSG's strong reputation in the marketplace is the result of longstanding relationships with its customers and business partners.

Customers

OSG's customers include major independent and state-owned oil companies, oil traders, refinery operators and U.S. and international government entities. The Company believes that it distinguishes itself in the shipping market through an emphasis on service, safety and reliability and its ability to maintain and grow long-term customer relationships.

Employees

As of December 31, 2011, the Company had approximately 3,600 employees comprised of 3,170 seagoing personnel and 430 shore side staff. The Company has collective bargaining agreements with three different U.S. maritime unions covering 743 seagoing personnel employed on the Company's U.S. Flag vessels. These agreements are in effect for periods ending between March 2012 and June 2020. Under the collective bargaining agreements, the Company is obligated to make contributions to pension and other welfare programs. The Company also has collective bargaining agreements with seven other maritime unions covering 2,270 seagoing personnel employed on the Company's International Flag vessels. These agreements are in effect through December 2014. OSG believes that it has a satisfactory relationship with its employees.

FORWARD-LOOKING STATEMENTS

This Form 10-K contains forward looking statements regarding the outlook for tanker and articulated tug/barge markets, and the Company's prospects, including prospects for certain strategic alliances and investments. All statements other than statements of historical facts should be considered forward-looking statements. There are a number of factors, risks and uncertainties, many of which are beyond the control of the Company, that could cause actual results to differ materially from the expectations expressed or implied in these forward looking statements, including changes in production of or demand for oil and petroleum products, either globally or in particular regions; greater than anticipated levels of newbuilding orders or less than anticipated rates of scrapping of older vessels; changes in trading patterns for particular commodities significantly impacting overall tonnage requirements; changes in the global economy and various regional economies; risks incident to vessel operation, including accidents and discharge of pollutants; unanticipated changes in laws and regulations; increases in costs of operation; drydocking schedules differing from those previously anticipated; the ability of the Company to attract and retain experienced, qualified and skilled crewmembers; changes in credit risk of counterparties, including shipyards, suppliers and financial lenders, and of joint venturers, partners and charterers; delays (including failure to deliver) or cost overruns in the building of new vessels or the conversion of existing vessels for other uses; the cost and availability of insurance coverage; the availability to the Company of suitable vessels for acquisition or chartering-in on terms it deems favorable; changes in the pooling arrangements in which the Company participates, including withdrawal of participants or termination of such arrangements; constraints on capital availability adversely affecting the tanker industry generally and the Company’s ability to replace or refinance its existing credit facilities; changes in the market value of vessels, which could adversely affect the Company’s compliance with certain of its financial covenants; changes in U.S. income tax law relating to the deferral of taxes on shipping income of the Company’s foreign subsidiaries; limitation on the commercial acceptability of vessels older than a specified age, even if they have been recently rebuilt; estimates of future costs and other liabilities for certain environmental matters and compliance plans; and projections of the costs needed to develop and implement the Company's strategy of being a market leader in the segments in which the Company competes. The Company assumes no obligation to update or revise any forward looking statements. Forward looking statements in this Form 10-K and written and oral forward looking statements attributable to the Company or its representatives after the date of this Form 10-K are qualified in their entirety by the cautionary statement contained in this paragraph and in other reports hereafter filed by the Company with the Securities and Exchange Commission.

OPERATIONS

The bulk shipping of crude oil and refined petroleum products has many distinct market segments based, in large part, on the size and design configuration of vessels required and, in some cases, on the flag of registry. Freight rates in each market segment are determined by a variety of factors affecting the supply and demand for suitable vessels. Tankers, ATBs and Product Carriers are not bound to specific ports or schedules and therefore can respond to market opportunities by moving between trades and geographical areas. The Company has established three reportable business segments: International Crude Tankers, International Product Carriers, and U.S. vessels.

The following chart reflects the percentage of TCE revenues generated by the Company's three reportable segments for each year in the three-year period ended December 31, 2011 and excludes the Company's proportionate share of TCE revenues of affiliated companies.

	Percentage of TCE Revenues					
	2011		2010		2009	
International						
Crude Tankers	33.7	%	49.6	%	51.2	%
Product Carriers	25.3	%	22.1	%	23.7	%
Other	1.7	%	1.4	%	0.8	%
Total International Segments	60.7	%	73.1	%	75.7	%
U.S.	39.3	%	26.9	%	24.3	%
Total	100.00	%	100.0	%	100.0	%

The following chart reflects the percentage of income/(loss) from vessel operations accounted for by each reportable segment. Results from vessel operations is before general and administrative expenses, severance and relocation costs, shipyard contract termination costs, gain/(loss) on disposal of vessels, impairment charges (vessel and goodwill) and the Company's share of income from affiliated companies.

	Percentage of Income/(loss) from Vessel Operations		
	2011	2010	2009
International			
Crude Tankers	(116.3)%	130.6 %	81.2 %
Product Carriers	(56.1)%	(35.1)%	(3.2)%
Other	(1.4)%	(1.2)%	(1.4)%
Total International Segments	(173.8)%	94.3 %	76.6 %
U.S.	73.8 %	5.7 %	23.4 %
Total	(100.0)%	100.0 %	100.0 %

For additional information regarding the Company's three reportable segments for the three years ended December 31, 2011, and reconciliations of (i) time charter equivalent revenues to shipping revenues and (ii) income/(loss) from vessel operations for the segments to income/(loss) before income taxes, as reported in the consolidated statements of operations, see Management's Discussion and Analysis of Financial Condition and Results of Operations set forth in Item 7, and Note 4 to the Company's consolidated financial statements set forth in Item 8.

Charter Types

The Company believes that by balancing the mix of TCE revenues generated by voyage charters and time charters, the Company is able to maximize its financial performance throughout shipping cycles.

Spot Market

Voyage charters, including vessels operating in Commercial Pools that predominantly operate in the spot market, constituted 65% of the Company's TCE revenues in 2011, 64% in 2010 and 49% in 2009. Accordingly, the Company's shipping revenues are significantly affected by prevailing spot rates for voyage charters in the markets in which the Company's vessels operate. Spot market rates are highly volatile. Rates are determined by market forces such as local and worldwide demand for the commodities carried (such as crude oil or petroleum products), volumes of trade, distances that the commodities must be transported, and the amount of available tonnage both at the time such tonnage is required and over the period of projected use and the levels of seaborne and shore-based inventories of crude oil and refined products. Seasonal trends affect world oil consumption and consequently vessel demand. While trends in consumption vary with seasons, peaks in demand quite often precede the seasonal consumption peaks as refiners and suppliers try to anticipate consumer demand. Seasonal peaks in oil demand have been principally driven by increased demand prior to Northern Hemisphere winters, as heating oil consumption increases, and increased demand for gasoline prior to the summer driving season in the U.S. Available tonnage is affected over time, by the volume of newbuilding deliveries, the number of tankers used to store clean products and crude oil, and the removal (principally through scrapping or conversion) of existing vessels from service. Scrapping is affected by the level of freight rates; scrap prices; vetting standards established by charterers and terminals; and by international and U.S. governmental regulations that establish maintenance standards and mandate the retirement of vessels lacking double hulls.

Time and Bareboat Charter Market

The Company's U.S. Flag tanker fleet, the LNG fleet and the two FSOs include a number of vessels that operate on time charters, providing a predictable level of revenues, which is not subject to fluctuations inherent in spot-market rates. During the two years ended December 31, 2010, the Company entered into Forward Freight Agreements ("FFAs") and related bunker swaps as hedges for reducing the volatility of earnings from operating the Company's VLCCs in the spot market. These derivative instruments seek to create synthetic time charters. The impact of these derivatives, which qualify for hedge accounting treatment, is reported together with time charters in the physical market. Time and bareboat charters constituted 35% of the Company's TCE revenues in 2011, 36% in 2010 and 51% in 2009. Because of the depressed market conditions existing between 2009 and 2011, the Company has been unable to replace expiring term business at comparable levels. Although medium-term time charters are available in the Product Carrier markets, management has not deemed the rates offered by charterers to be sufficiently attractive to warrant entering into such business.

Fleet Summary

As of December 31, 2011, OSG’s operating fleet consisted of 111 vessels, 59% of which were owned, with the remaining vessels bareboat or time chartered-in. Vessels chartered-in may be Bareboat Charters (where OSG is responsible for all Vessel Expenses) or Time Charters (where the shipowners are responsible for all Vessel Expenses). The Company’s fleet list excludes vessels chartered-in where the duration of the charter was one year or less at inception. A detailed fleet list and updates on vessels under construction can be found in the Fleet section on www.osg.com.

	Vessels Owned		Vessels Chartered-in	
Vessel Type	Number	Weighted by Ownership	Number	Weighted by Ownership
Operating Fleet				
FSO	2	1.0	-	
VLCC and ULCC	10	10.0	4	
Suezmax	-	-	2	
Aframax	6	6.0	3	
Panamax	9	9.0	-	
Lightering	2	2.0	4	
Total International Flag Crude Tankers	29	28.0	13	
LR1	4	4.0	2	
MR[1]	15	15.0	20	
Total International Flag Product Carriers	19	19.0	22	
Chemical Carrier	-	-	1	
Car Carrier	1	1.0	-	
Total Int’l Flag Operating Fleet	49	48.0	36	

We acquired SpinVox Limited (SpinVox), a UK-based privately-held company engaged in t providing voice to text services, on December 30, 2009 and other businesses during the second quarters of 2010. Refer to Note 4 for additional information.

Although we believe the disclosures in these financial statements are adequate to make the info presented not misleading, certain information normally included in the footnotes prepared in ac GAAP has been omitted. Accordingly, these financial statements should be read in conjunction financial statements and the notes thereto included in our Annual Report on Form 10-K for the September 30, 2009. Interim results are not necessarily indicative of the results that may be exp year.

We reclassified certain acquisition-related costs included within operating expenses for the thre months ended June 30, 2009 to conform to our revised statement of operations presentation for disclosed in Note 2 below. Such reclassifications had no impact on earnings or cash flows prov operations.

2. Summary of Significant Accounting Policies

We have made no material changes to the significant accounting policies disclosed in our Annu Form 10-K for the fiscal year ended September 30, 2009, other than as outlined below.

Acquisition-Related Costs, net

Acquisition-related costs include those costs related to business and other acquisitions, includir acquisitions. These costs consist of transition and integration costs, including retention paymen employee costs and earn-out payments treated as compensation expense, as well as the costs of integration-related services provided by third-parties; professional service fees, including direc of the transaction and post-acquisition legal and other professional service fees associated with regulatory matters related to acquired entities; and adjustments to acquisition-related items that be marked to fair value each reporting period, such as contingent consideration, and other item acquisitions for which the measurement period has ended. Previous to our adoption of ASC 80 *Combinations* (formerly referred to as SFAS No. 141 (revised), *Business Combinations* (SFA 2010, certain acquisition-related costs and adjustments now recorded as operating expenses in statements of operations were included as a part of the consideration transferred and capitalized accounting for our business acquisitions pursuant to previous accounting rules, primarily direct costs. In addition, there were no items under the legacy business combination accounting guida required to be re-measured to fair value on a recurring basis.

	Three Months Ended June 30,		Nine M
	2010	2009	2010
Transition and integration costs	$ 3,383	$ 1,243	$ 12,03
Professional service fees	3,079	3,361	14,93
Acquisition-related adjustments	(337)	55	(7
Total	$ 6,125	$ 4,659	$ 26,89

Accounting for Collaboration Agreements

On October 9, 2009, we entered into a five-year collaboration agreement with a third party to a development of new speech technologies. All intellectual property derived from the collaborati jointly-owned by the two parties and Nuance will have the sole rights to commercialize the inte during the term of the agreement. In consideration for the services from the third party in the co efforts, as well as the joint ownership rights over intellectual property developed under the arra exclusive right to commercialize such developed intellectual property for the term of the arrang pay $80.0 million in five equal payments of $16.0 million on August 15th of each year, payabl common stock, at our option. These upfront payments will be recorded as a prepaid asset and e over each annual period, commensurate with the pattern in which we expect the third party to p services and convey our rights under the arrangement. On October 14, 2009, we made our first the arrangement consisting of 1,047,120 shares of our common stock valued at $16.0 million. F nine months ended June 30, 2010, $4.0 million and $12.0 million, respectively have been recor and development expense in our consolidated statements of operations.

On January 13, 2010, we amended the collaboration agreement to extend certain provisions for following the termination of the agreement. In consideration for the extension, we agreed to pa $12.0 million to the third-party in five equal payments of $2.4 million on August 15th of each y five-year agreement term, payable in cash or our common stock, at our option, with the excepti payment, which was made during the second quarter of fiscal 2010 through the issuance of 145 our common stock. These upfront payments are recorded as a prepaid asset when made and wil ratably to sales and marketing expense over the eighteen-month extension period.

Accounting for Convertible Debt

During the first quarter of fiscal 2010, we adopted the provisions in FASB ASC 470-20 as they convertible debt instruments that may be settled in cash upon conversion (formerly referred to 14-1, *Accounting for Convertible Debt Instruments that May be Settled in Cash upon Conversi Partial Cash Settlement)*) effective October 1, 2009. The guidance requires us to separately acc liability (debt) and equity (conversion option) components of our convertible debt instruments permit settlement in cash upon conversion in a manner that reflects our nonconvertible debt bo the time of issuance. The equity components of our convertible debt instruments are recorded t equity with an offsetting debt discount. The debt discount created is amortized to interest exper consolidated statement of operations using the effective interest method over the expected term convertible debt. The provisions herein discussed have been applied retrospectively to all finan presented. Refer to information below and in Note 12 for further information.

NUANCE COMMUNICATIONS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (C

The following tables illustrate the retrospective effect of adopting ASC 470-20 to the consolida operations for the three and nine months ended June 30, 2009 (in thousands):

	Three Months Ended June 30, 2009		Nine Mont June 30
	As Originally Reported	As Adjusted for Retrospective Application	As Originally Reported
Interest expense	$ 8,331	$ 10,137	$ 31,466
Income (loss) before income taxes	5,661	3,855	(1,209)
Net loss	(1,009)	(2,815)	(18,492)
Net loss per share Basic and Diluted	$ (0.00)	$ (0.01)	$ (0.07)

The following table illustrates the retrospective effect of adopting ASC 470-20 to the consolida as of September 30, 2009 (in thousands):

	As Originally Reported	A
Other assets(a)	$ 52,511	
Long-term portion of debt and capital leases(b)	888,611	
Additional paid-in-capital(c)	2,254,511	
Accumulated deficit	$ (247,338)	

(a) Other assets have been adjusted for the portion of the debt issuance costs attributable to th 2.75% Convertible Senior Notes that must be retrospectively allocated to the equity comp instrument through additional paid-in-capital as of the date of the notes issuance.

(b) Long-term portion of debt and capital leases has been adjusted to reflect retrospective rec debt discount created by bifurcating the equity component of the convertible notes from th component.

(c) Additional paid-in-capital has been adjusted to reflect recording, retrospectively, the equit the convertible notes, as well as the equity component allocation of the debt issuance cost the 2.75% Convertible Senior Notes.

Recently Issued Accounting Standards

In April 2010, the FASB issued ASU No. 2010-17, *Revenue Recognition Milestone Method (*
Milestone Method of Revenue Recognition. The ASU codifies the consensus reached in Emergi
Force (EITF) Issue No. 08-9, *Milestone Method of Revenue Recognition*. The amendments t
Accounting Standards Codification (the Codification or ASC) provide guidance on defin
determining when it may be appropriate to apply the milestone method of revenue recognition
development transactions. Consideration that is contingent on achievement of a milestone in its
recognized as revenue in the period in which the milestone is achieved only if the milestone is
certain criteria to be considered substantive. The amendments in the ASU are effective on a pro
for milestones achieved in fiscal years, and interim periods within those years, beginning on or
2010. Early adoption is permitted. If an entity elects early adoption and the period of adoption
beginning of the entity s fiscal year, the entity must apply the amendments retrospectively fro
the year of adoption. Entities may also elect to adopt the amendments in the ASU retrospective
periods. We are currently evaluating the potential impact of this ASU on our consolidated finan

In January 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-06, *Impr*
about Fair Value Measurements (Topic 820) Fair Value Measurements and Disclosures (A

NUANCE COMMUNICATIONS, INC.

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additional disclosures about the different classes of assets and liabilities measured at fair value, techniques and inputs used, the activity in Level 3 fair value measurements, and transfers betw and 3. Levels 1, 2 and 3 of fair value measurements are defined in Note 8 below. ASU 2010-06 for us for the interim reporting period beginning January 1, 2010, except for the provisions rela Level 3 fair value measurements. Those provisions are effective for fiscal years beginning afte 2010, and for interim periods within those fiscal years. ASU 2010-06 impacts disclosure only a not, and is not expected to, have a material impact on our financial statements.

In September 2009, the EITF ratified EITF Issue No. 08-1, *Revenue Arrangements with Multip* which has since been codified in the ASC as ASU No. 2009-13 (ASU 2009-13), supersedes No. 00-21, *Revenue Arrangements with Multiple Deliverables*, now referred to as ASC 605-25- 2009-13 eliminates the residual method of accounting for non-software arrangements, as well a requirements for establishing objective and reliable evidence of fair value. The residual method ASU 2009-13 by the estimated selling price method whereby revenue in a multiple-element ar allocated to each element based on its estimated selling price. Estimating selling price is establ hierarchy starting with vendor-specific objective evidence of fair value, followed by third-party lastly by any reasonable, objective estimate of the selling price were the element to be sold on a basis. Estimates of selling price must consider both entity-specific factors and market conditio is applied prospectively to all revenue transactions entered into or materially modified in fiscal on or after June 15, 2010. Early adoption is permitted if adopted as of the beginning of an entit no prior interim period financial statements from that fiscal year have already been issued or th retrospectively applies the provisions of this ASU to its previously-issued current fiscal year in statements. We currently do not expect that the adoption of ASU 2009-13 will have a material consolidated financial statements.

In September 2009, the EITF ratified EITF Issue No. 09-3, *Applicability of AICPA Statement o Certain Arrangements That Include Software Elements*, which has since been codified in the C ASU No. 2009-14 (ASU 2009-14). ASU 2009-14 applies to multiple-element arrangements software and hardware elements, and amends the scope of AICPA Statement of Position (SO *Software Revenue Recognition*, now referred to as ASC 985-605, to exclude tangible products software and non-software components that together function to deliver the product s essentia the scope of ASC 985-605. ASU 2009-14 is applied prospectively to all revenue transactions e materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is perm ASU 2009-13 is also early adopted as of the same period. We are continuing to evaluate the po this ASU on our consolidated financial statements.

3. Comprehensive Income (Loss)

The components of comprehensive income (loss) are as follows (table in thousands):

	Three Months Ended June 30,		Nine M J
	2010	2009	2010

Net loss	$ (1,530)	$ (2,815)	$ (21,204
Other comprehensive income (loss):			
Foreign currency translation adjustment	(19,488)	15,786	(31,510
Unrealized gain (loss) on cash flow hedge derivatives	690	1,434	2,228
Total comprehensive income (loss)	$ (20,328)	$ 14,405	$ (50,486

4. Business Acquisitions

Acquisition of SpinVox

On December 30, 2009, we acquired all of the outstanding capital stock of SpinVox Limited (
UK-based privately-held company engaged in the business of providing voicemail-to-text servi
acquisition was a taxable stock purchase and the goodwill resulting from this acquisition is not
deductible for tax purposes. The results of operations of SpinVox have been included in our res
operations from January 1, 2010. The results of operations of SpinVox for the one day, Decem
the fiscal first quarter during which SpinVox was a part of Nuance were excluded from our cor
for the nine months ended June 30, 2010 as such amounts for that one day were immaterial.

A summary of the preliminary allocation of the purchase consideration is as follows (in thousa

Total purchase consideration:
Cash
Common stock(a)

Total purchase consideration

Allocation of the purchase consideration:
Cash
Accounts receivable(b)
Other assets
Property and equipment
Identifiable intangible assets
Goodwill

Total assets acquired
Current liabilities(c)
Deferred revenue

Total liabilities assumed

Net assets acquired

(a) Approximately 2.3 million shares of our common stock, valued at $15.81 per share based
price of our common stock on the acquisition date, were issued at closing.

(b) Accounts receivable have been recorded at their estimated fair value, which consists of the
receivable assumed of $16.6 million, reduced by fair value reserve of $5.5 million represe
of contractually owed accounts receivable which we do not expect to be collectible.

(c) Current liabilities include a commitment of EUR 25.0 million ($36.0 million based on the 2009 exchange rate) fixed obligation, payable in cash, in December 2010.

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The following are the identifiable intangible assets acquired and their respective weighted aver
as determined based on a preliminary valuation (table in thousands, except for years):

	Amount	Weig
Customer relationships	$ 23,400	
Core and completed technology	8,400	
Trade name	600	
Total	$ 32,400	

Other Fiscal 2010 Acquisitions

During fiscal 2010, we acquired several businesses primarily to expand our product offerings a
technology base. The results of operations of these companies have been included in our conso
from their respective acquisition dates. The total consideration for these acquisitions was $35.2
including the issuance of 1.2 million shares of our common stock valued at $21.8 million. In al
purchase consideration for these acquisitions based on estimated fair values, we preliminarily r
$21.5 million of goodwill and $13.8 million of identifiable intangible assets. The preliminary a
purchase consideration were based upon preliminary valuations and our estimates and assumpt
to change. Intangible assets acquired included primarily core and completed technology and cu
relationships with weighted average useful lives of 7.2 years. The acquisitions were primarily s
and the goodwill resulting from these acquisitions is not expected to be deductible for tax purp

Pro Forma Results

The following unaudited pro forma financial information summarizes the combined results of o
Company and SpinVox as though they were combined from October 1, 2008 (table in thousanc
share data):

	Three Months Ended June 30,		Nine Mo Ju
	2010	2009	2010
Revenue	$ 273,203	$ 247,728	$ 821,161
Net loss	(1,530)	(17,271)	(52,766)
Net loss per share basic and diluted	$ (0.01)	$ (0.07)	$ (0.18)

We have not furnished pro forma financial information relating to our other fiscal 2010 acquisi
such information is not material, individually or in the aggregate, to our financial results.

5. Contingent Acquisition Payments

Earn-out Payments

In accordance with our adoption of ASC 805 in fiscal 2010, for business combinations occurrin
the adoption date, the fair value of any contingent consideration will be established at the acqui
recorded as purchase price. The contingent consideration will then be adjusted to fair value eac
period and such adjustment will be recorded as an increase or decrease in current earnings. Co
consideration related to acquisitions prior to our adoption of ASC 805 have been and will conti
recorded as additional purchase price when the contingency is resolved and additional conside
attributable.

In connection with an immaterial acquisition during fiscal 2010, we agreed to make contingent
payments of up to $2.5 million, payable in stock, upon the achievement of certain financial targ

acquisition date, we recorded $1.0 million as contingent consideration. For the three and nine n June 30, 2010, we have recorded income of $0.4 million and $0.2 million, respectively, as fair adjustments included in acquisition-related costs, net in our consolidated statement of operatio

In connection with our acquisition of SNAPin Software, Inc. (SNAPin), we agreed to make earn-out payment of up to $45.0 million in cash to be paid, if at all, based on the business achie performance targets that are measurable from the acquisition date to December 31, 2009. In Ap Company and the former shareholders of SNAPin agreed on a final earn-out payment of $21.2 issued 593,676 shares of our common stock, valued at $10.2 million, as our first payment unde agreement. The remaining balance is payable in cash or stock, solely at our option, on or befor and is included in long-term liabilities as of June 30, 2010.

In connection with our acquisition of Multi-Vision Communications, Inc. (Multi-Vision), w contingent earn-out payments of up to $15.0 million, payable in stock, or cash, solely at our dis to earn-out provisions described in the share purchase agreement. We have notified the former Multi-Vision that the performance targets were not achieved. Through June 30, 2010, we have obligation or related compensation expense relative to these measures.

In connection with our acquisition of Vocada, Inc. (Vocada), we agreed to make contingent of up to $21.0 million, payable in stock, or cash, solely at our discretion, upon the achievement financial targets measured over defined periods through December 31, 2010. Earn-out paymen recorded as incremental purchase price and allocated to goodwill. We have notified the former Vocada that the financial targets for certain periods were not achieved and they have requested information regarding this determination. We are currently in discussions with the former shar Vocada regarding this matter. Through June 30, 2010, we have not recorded any earn-out oblig the Vocada acquisition.

In connection with the acquisition of Commissure, Inc. (Commissure), we agreed to make c payments of up to $8.0 million, payable in stock, or cash, solely at our discretion, upon the ach certain financial targets for the fiscal years 2008, 2009 and 2010. Earn-out payments, if any, w incremental purchase price and allocated to goodwill. We have notified the former shareholder that the financial targets for the fiscal years 2008 and 2009 were not achieved and the related c earn-out payment was not earned. Through June 30, 2010, we have not recorded any earn-out c to the Commissure acquisition.

In November 2008, we amended the earn-out provisions set forth in the merger agreement rela acquisition of Mobile Voice Control, Inc. (MVC) such that the former shareholders of MVC earn 377,964 and 755,929 shares based on the achievement of calendar 2008 and 2009 financia respectively. Earn-out payments, if any, will be recorded as incremental purchase price and all goodwill. We have notified the former shareholders of MVC that the financial targets for calen 2009 were not achieved and therefore we have not recorded any obligation relative to these me

In connection with our acquisition of Phonetic Systems Ltd. (Phonetic) in February 2005, w contingent earn-out payments of $35.0 million upon achievement of certain established financi performance targets, in accordance with the merger agreement. In December 2009, we paid $1

former shareholders of Phonetic in final settlement of the contingent earn-out provisions; recor
paid as additional purchase price related to the Phonetic acquisition.

Escrow and Holdback Arrangements

In connection with certain of our acquisitions, we have placed either cash or shares of our com
escrow to satisfy any claims we may have. If no claims are made, the escrowed amounts will b
former shareholders of the acquired companies. Historically, under the previous accounting gu

SFAS No. 141, *Business Combinations* (SFAS 141), we could not make a determination, be doubt, whether the escrow would become payable to the former shareholders of these compani escrow period had expired. Accordingly, these amounts were treated as contingent purchase pr determined that the escrow was payable, at which time the escrowed amounts would be record purchase price and allocated to goodwill. Under the revised accounting guidance of ASC 805, are generally considered part of the initial purchase consideration and accounted for as goodwi

The following table summarizes the terms of the escrow arrangements that were entered into u of SFAS 141 that were not released as of June 30, 2010 (table in thousands):

	Initially Scheduled Escrow Release Date
X-Solutions Group B.V.	December 10, 2010
eCopy, Inc.	December 30, 2010
Total	

6. Goodwill and Intangible Assets

The changes in the carrying amount of goodwill for the nine months ended June 30, 2010, are thousands):

Balance as of September 30, 2009
Goodwill acquired
Purchase accounting adjustments
Effect of foreign currency translation
Balance as of June 30, 2010

Purchase accounting adjustments recorded during the nine months ended June 30, 2010 consist $13.1 million increase due to change in the fair value estimate of acquired intangible assets fro quarter fiscal 2009 acquisition, a $11.3 million increase related to Phonetic earn-out payment, increase to the SNAPin earn-out liability based on final earn-out value discussed in Note 5 abo $3.7 million release of escrow cash after the satisfaction of certain pre-acquisition tax related c increases were partially offset by a $1.9 million reduction to the Philips Speech Recognition Sy (PSRS) purchase price based on a final working capital adjustment agreed between us and t shareholder of PSRS in November 2009.

Intangible assets consist of the following as of June 30, 2010 (table in thousands, except for ye

	June 30, 2010		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	$ 573,059	$ (212,361)	$ 360,698
Technology and patents	369,034	(118,323)	250,711
Tradenames, trademarks, and other	38,641	(11,629)	27,012
Non-competition agreements	4,567	(2,909)	1,658
Subtotal	985,301	(345,222)	640,079
Tradename, indefinite life	27,800		27,800
Total	$ 1,013,101	$ (345,222)	$ 667,879

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In June 2009, we entered into a joint marketing and selling agreement with a third party and pa consideration of the arrangement. We have capitalized the $7.0 million payment as an intangib in the tradenames, trademarks, and other grouping above, and assigned a useful life of 3 years, with the legal term of the rights in the arrangement. In addition to the $7.0 million paid in June issued 879,567 shares of our common stock, valued at $13.0 million, in December 2009 as an a payment, upon the third party meeting certain performance criteria under the agreement by Oct The additional $13.0 million was capitalized and classified in the same manner as the initial $7 payment.

In March 2010, we acquired a portfolio of technology patents as well as a royalty-free, paid-up and object code license from third-parties for $12.5 million, including $2.5 million in cash and of our common stock valued at $10.0 million. The estimated useful lives of the patent portfolio license are 13 years and 7 years, respectively. Both the patent portfolio and the license have be within the technology and patents grouping above.

In June 2010, we acquired a perpetual source and object code license from a third-party for $7. estimated useful life of the license is approximately 13 years. The license has been included wi technology and patents grouping above.

Estimated amortization expense for each of the five succeeding years and thereafter, is as follo thousands):

Year Ending September 30,	Cost of Revenue	Operating Expenses
2010 (July 1, 2010 to September 30, 2010)	$ 12,372	$ 21,42
2011	48,459	79,67
2012	44,213	69,40
2013	38,355	54,98
2014	29,854	48,22
Thereafter	77,458	115,64
Total	$ 250,711	$ 389,36

7. Financial Instruments and Hedging Activities

Interest Rate Swap Agreements

To manage the interest rate exposure on our variable-rate borrowings, we use interest rate swa specific variable-rate debt into fixed-rate debt. As of June 30, 2010, we have two outstanding i designated as cash flow hedges with an aggregate notional amount of $200 million. The interes swaps are 2.7% and 2.1%, plus the applicable margin for the Credit Facility, and they expire in and November 2010, respectively. As of June 30, 2010 and September 30, 2009, the aggregate unrealized losses related to these swaps, were $1.5 million and $4.0 million, respectively and w accumulated other comprehensive income (loss) in the accompanying balance sheets.

Forward Currency Contracts Designated as Cash Flow Hedges

On October 1, 2009, we entered into foreign currency contracts to hedge exposure on the varial flows in Canadian dollars with a total notional amount of CAD$8.7 million. These contracts ar cash flow hedges. At June 30, 2010, one contract with an unsettled notional amount of CAD$0 ($0.3 million based on the June 30, 2010 exchange rate) remained outstanding and was settled As of June 30, 2010, the aggregate cumulative unrealized gains related to these contracts were

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In February and April 2010, we entered into foreign currency contracts to hedge exposure on th cash flows in Hungarian Forints (HUF) with a total notional amount of HUF 997.0 million. designated as cash flow hedges. At June 30, 2010, these contracts had an aggregate remaining, notional amount of HUF 403.0 million ($1.7 million based on the June 30, 2010 exchange rate) settle monthly through December 2010. As of June 30, 2010, the aggregate cumulative unrealiz to these contracts were immaterial.

Other Derivative Activities

During the three months ended December 31, 2008, we entered into foreign currency forward c foreign currency exposure on the deferred acquisition payment of 44.3 million related to our a PSRS, resulting in a net gain during that period of $8.0 million included in other income (exper currency contracts matured and were settled on October 22, 2009. The gain for the period from 2009 to settlement on October 22, 2009 was $1.6 million, but was offset in other income (expe loss resulting from the corresponding change in the associated deferred acquisition payment lia

In June 2009, we acquired certain intangible assets and issued 1,809,353 shares of our commor $25.0 million, as part of the total consideration. We also issued an additional 315,790 shares of stock, valued at $4.5 million, in June 2009 as a prepayment for professional services. The share subject to security price guarantees which are accounted for as derivatives, and are being accou separately from their host agreements due to the determination that such instruments would not equity instruments if freestanding. The security price guarantees require a payment from either party, or from the third party to us based upon the difference between the price of our common issue date and an average price of our common stock approximately six months following the i Changes in fair value of these security price guarantees are reported in earnings each period as income (expense) within other income (expense), net. These security price guarantees expired a in December 2009 and January 2010. The third-party paid $3.8 million to the Company during final settlement.

In October and December 2009, we issued 1,047,120 and 879,567 shares of our common stock third party, valued at $16.0 million and $13.0 million, respectively. The $16.0 million payment payment in consideration for the research and development services of the third party in conne five-year collaboration arrangement discussed in Note 2 above, while the $13.0 million paymen payment in respect of the joint marketing and selling agreement with the same third party discu above. These shares are subject to security price guarantees of the same nature as those describ third-party paid $2.6 million and $0.9 million in April 2010 and July 2010, respectively, to the final settlement of these two security price guarantees.

In March 2010, we issued 607,903 and 145,897 shares of our common stock in payment to a th at $10.0 million and $2.4 million, respectively. The $10.0 million payment was for the purchas and object code software license discussed in Note 6 above, while the $2.4 million payment wa the amendment of the five-year collaboration agreement discussed in Note 2 above. These shar security price guarantees of the same nature as those described above.

In June 2010, we issued 152,440 shares of our common stock in payment to a third party. Thes subject to security price guarantees of the same nature as those described above.

As of June 30, 2010, we have outstanding security price guarantees relative to a total of 1,785,8 common stock issued to a third party. For the three and nine months ended June 30, 2010, we r decrease in fair value of $1.0 million and an increase in fair value of $3.7 million, respectively, settled and unsettled security price guarantees within other income (expense), net in the consol of operations.

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The following table provides a quantitative summary of the fair value of our hedged and non-h instruments as of June 30, 2010 and September 30, 2009 (table in thousands):

		Fair
Description	**Balance Sheet Classification**	**June 30, 2010**
Derivatives Not Designated as Hedges:		
Foreign currency contracts	Prepaid expenses and other current assets	$
Security price guarantees	Prepaid expenses and other current assets	915
Security price guarantees	Accrued expenses and other current liabilities	(1,343)
Net asset (liability) value of non-hedged derivative instruments		$ (428)
Derivatives Designated as Hedges:		
Foreign currency contracts	Prepaid expenses and other current assets	$ 9
Foreign currency contracts	Accrued expenses and other current liabilities	(298)
Interest rate swaps	Accrued expenses and other current liabilities(a)	(1,465)
Net asset (liability) value of hedged derivative instruments		$ (1,754)

(a) The fair value of the interest rate swaps was classified in other long-term liabilities as of S 2009 as the settlement date for the swaps was greater than twelve months from the balanc

The following tables summarize the activity of derivative instruments for fiscal 2010 and 2009 thousands):

Derivatives Designated as Hedges for the Three Months Ended June 30,

	Amount of Gain (Loss) Recognized in OCI	**Location and Amount of Reclassified fro**

			Accumulated OCI into Inc	
			Portion)	
	2010	**2009**		**201**
Foreign currency contracts	$ (321)	$ 544	Other income (expense), net	$ (9
Interest rate swaps	$ 1,109	$ 700	N/A	$

Derivatives Designated as Hedges for the Nine Months Ended June 30,

			Location and Amount of	
	Amount of Gain (Loss)		**Reclassified fro**	
			Accumulated OCI into Inc	
	Recognized in OCI		**Portion)**	
	2010	**2009**		**201**
Foreign currency contracts	$ (99)	$ 158	Other income (expense), net	$ (1
Interest rate swaps	$ 2,517	$ (3,143)	N/A	$

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Derivatives Not Designated as Hedges

		Amount of Gain (Loss) Reco		
		Three Months Ended		**Nine**
	Location of Gain (Loss)	**June 30,**		
	Recognized in Income	**2010**	**2009**	**201**
Foreign currency contracts	Other income (expense), net	$	$3,721	$
Security price guarantees	Other income (expense), net	$ (1,044)	$(3,782)	$ 3,6

Other Financial Instruments

Financial instruments, including cash equivalents, restricted cash, accounts receivable, and deri instruments, are carried in the consolidated financial statements at amounts that approximate th Refer to Note 12 for discussion of fair value of our long-term debt.

8. Fair Value Measures

Fair value is defined as the price that would be received for an asset, or paid to transfer a liabili transaction between market participants at the measurement date. Valuation techniques must m of observable inputs and minimize the use of unobservable inputs. When determining the fair v measurements for assets and liabilities required to be recorded at fair value, we consider the pri advantageous market in which we would transact and consider assumptions that market partici when pricing the asset or liability, such as inherent risk, transfer restrictions, and risk of nonpe

ASC 820 (formerly referred to as SFAS No. 157, *Fair Value* Measurements) establishes a valu on three levels of inputs, of which the first two are considered observable and the third is consi unobservable:

Level 1. Quoted prices for identical assets or liabilities in active markets which we can a

Level 2. Observable inputs other than those described as Level 1.

Level 3. Unobservable inputs.

Assets and liabilities measured at fair value on a recurring basis at June 30, 2010 consisted of (thousands):

	June 30, 2010		
	Level 1	**Level 2**	**Level 3**

Assets:			
Money market funds(a)	$ 424,331	$	$
US government agency securities(a)	10,000		
Foreign currency exchange contracts(b)		9	
Total assets at fair value	$ 434,331	$ 9	$
Liabilities:			
Foreign currency exchange contracts(b)	$	$ 298	$
Security price guarantees(c)		428	
Contingent consideration(d)			80
Interest rate swaps(e)		1,465	
Total liabilities at fair value	$	$ 2,191	$ 80

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(a) Money market funds and US government agency securities, included in cash and cash equ accompanying balance sheet, are valued at quoted market prices in active markets.

(b) The fair value of our foreign currency exchange contracts is the intrinsic value of the cont observable inputs for similar derivative instruments in active markets or quoted prices for similar instruments in markets that are not active or are directly or indirectly observable.

(c) The fair values of the security price guarantees are determined using a modified Black-Sc derived from observable inputs such as US treasury interest rates, our common stock price volatility of our common stock. The valuation model values both the put and call compon guarantees simultaneously, with the net value of those components representing the fair v instrument.

(d) The fair value of our contingent consideration arrangement is determined based on the Co evaluation as to the probability and amount of any earn-out that will be achieved based on performance by the acquired entity, as well as our common stock price since the continge arrangement is payable in shares of our common stock. Refer to Note 5 for additional info

(e) The fair values of the interest rate swaps are estimated using discounted cash flow analyse observable market inputs such as LIBOR based yield curves, forward rates, and credit s

Level 3 Instruments

As of June 30, 2010, only our contingent consideration arrangement, entered into during the se fiscal 2010, qualifies as a Level 3 instrument. Prior to the second quarter fiscal 2010, we have Level 3 instruments. $1.0 million of the fair value of the instrument was recorded as part of the transferred for one of our second quarter fiscal 2010 acquisitions. The remaining $0.2 million value between the acquisition date and June 30, 2010 is recorded as income in acquisition-rela our consolidated statements of operations.

9. Accrued Expenses and Other Current Liabilities

Accrued expenses consisted of the following (in thousands):

	June 30, 2010
Compensation	$ 56,122
Sales and marketing incentives(a)	35,600
Cost of revenue related liabilities	12,434
Professional fees	7,131
Income taxes payable	5,735
Sales and other taxes payable	5,619

Acquisition costs and liabilities	5,038
Deferred tax liability	1,578
Security price guarantees	1,343
Other	7,938
Total	$ 138,538

(a) Accrued sales and marketing incentives include a EUR 25.0 million ($30.5 million based o 2010 exchange rate) fixed obligation assumed in connection with our acquisition of SpinV in Note 4. During the third quarter of fiscal 2010, we placed EUR 18.0 million ($22.0 mill June 30, 2010 exchange rate) in an irrevocable standby letter of credit account. The fund i the payment of the fixed obligation, payable in cash, in December 2010 and has been reported as restricted ca accompanying balance sheets.

10. Accrued Business Combination Costs

The activity for the nine months ended June 30, 2010, relating to all facilities and personnel rec business combination costs, is as follows (in thousands):

	Facilities	Personne
Balance at September 30, 2009	$ 34,551	$ 2,49
Charged to goodwill	(15)	(75
Charged to restructuring and other charges, net	(527)	
Charged to interest expense	965	
Cash payments, net of sublease receipts	(8,465)	(1,59
Balance at June 30, 2010	$ 26,509	$ 14

	June 30, 2010
Reported as:	
Current	$ 9,574
Long-term	17,081
Total	$ 26,655

11. Restructuring and Other Charges, net

The following table sets forth the nine months ended June 30, 2010 accrual activity relating to other charges (in thousands):

	Personnel	Facilities	Other
Balance at September 30, 2009	$ 607	$ 310	$ 2
Restructuring and other charges, net	8,195	155	8,42
Non-cash adjustments			(6,83
Cash payments	(6,672)	(126)	(1,61
Balance at June 30, 2010	$ 2,130	$ 339	$

For the nine months ended June 30, 2010, we recorded net restructuring and other charges of $ which consisted primarily of $8.2 million related to the elimination of approximately 160 perso multiple functions within our company, including acquired entities, a $6.9 million write-off of capitalized patent defense costs as a result of unsuccessful litigation and $1.6 million of contrac costs.

12. Credit Facilities and Debt

At June 30, 2010 and September 30, 2009, we had the following borrowing obligations (in thou

	June 30, 2010
2.75% Convertible Debentures, net of unamortized discount of $38.5 million and $44.9 million, respectively	$ 211,477
Credit Facility	645,238
Obligations under capital leases	1,846
Other	48
Total long-term debt	858,609
Less: current portion	8,209
Non-current portion of long-term debt	$ 850,400

The estimated fair value of our long-term debt approximated $872.1 million at June 30, 2010 a at September 30, 2009. These fair value amounts represent the value at which our lenders coul within the financial markets, and do not represent the settlement value of these long-term debt each reporting date. The fair value of these long-term debt issues will continue to fluctuate eac fluctuations in market interest rates, and these fluctuations may have little to no correlation to debt balances. The decrease in fair value from September 30, 2009 to June 30, 2010 is generall the overall decline in the debt markets. The term loan portion of our Credit Facility is traded ar are based upon traded prices as of the reporting dates. The fair values of the 2.75% Convertible were estimated using the averages of the bid and ask trading quotes as of each respective repor no outstanding balance on the revolving credit line portion of our Credit Facility. Our capital le and other debt are not traded and the fair values of these instruments are assumed to approxima values as of June 30, 2010 and September 30, 2009.

2.75% Convertible Debentures

On August 13, 2007, we issued $250 million of 2.75% convertible senior debentures due in Au June 30, 2010, no conversion triggers were met. If the conversion triggers were met, we could repay all or some of the principal amount in cash prior to maturity.

Adoption of ASC 470-20

As discussed in Note 2 above, on October 1, 2009, we adopted ASC 470-20, which has been ap retrospectively to all periods presented in our consolidated financial statements. ASC 470-20 is 2.75% Convertible Debentures as we have the right to deliver cash in lieu of shares of our com combination of cash and shares of common stock, upon conversion for each of these issuances.

We recognized total interest expense of approximately $10.0 and $30.4 million during the thre
months ended June 30, 2010, respectively, and $10.1 and $36.8 million during the three and ni
June 30, 2009 related to the contractual interest coupon on all our outstanding long-term debt, a
debt issuance costs, and amortization of the discount on the liability component of our 2.75% C
Debentures. The effective interest rate on the liability component of our 2.75% Convertible De
including both the cash and non-cash interest components, was approximately 7% during the th
months ended June 30, 2010 and 2009. We are amortizing the discount on the liability compon
2.75% Convertible Debentures through August 2014, which is the first put date available to the
notes.

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The carrying amount of the equity component, principal amount of the liability component, una discount related to the liability component and net carrying amount of the liability component c subject to ASC 470-20 as of June 30, 2010 and September 30, 2009 were as follows (in thousa

	June 30, 2010
Carrying amount of equity component (conversion options)	$ 54,695
Principal amount of liability component	$ 250,000
Unamortized discount related to liability component	(38,523)
Net carrying amount of liability component	$ 211,477

Credit Facility

We have a credit facility which consists of a $75 million revolving credit line, reduced by outst credit, a $355 million term loan entered into on March 31, 2006, a $90 million term loan entere 2007 and a $225 million term loan entered into on August 24, 2007 (collectively the Credit Fa loans are due March 2013 and the revolving credit line is due March 2012. As of June 30, 2010 $15.9 million of letters of credit issued under the revolving credit line and there were no other c borrowings under the revolving credit line. As of June 30, 2010, we are in compliance with the the Credit Facility.

As of June 30, 2010, based on our leverage ratio, the applicable margin for our term loan was 1 rate borrowings and 2.00% for LIBOR-based borrowings. This results in an effective interest ra payments under the excess cash flow sweep provision were due in the first quarter of fiscal 201 cash flow, as defined, was generated in fiscal 2009. At the current time, we are unable to predic the outstanding principal, if any, that we may be required to repay in future fiscal years pursuan cash flow sweep provisions. If only the minimum required repayments are made, the annual ag amount of the term loans repaid would be as follows (table in thousands):

Year Ending September 30,
2010 (July 1, 2010 to September 30, 2010)
2011
2012
2013 (maturity)
Total

13. Net Income (Loss) Per Share

Common equivalent shares are excluded from the computation of diluted net income (loss) per effect is anti-dilutive. Potentially dilutive common equivalent shares aggregating to 19.9 millio 21.8 million shares for the three and nine months ended June 30, 2010, respectively, and 30.5 r 32.5 million shares for the three and nine months ended June 30, 2009, respectively, have been the computation of diluted net loss per share because their inclusion would be anti-dilutive.

14. Stockholders Equity

On March 19, 2004, we announced that Warburg Pincus had agreed to purchase all outstanding warrants for our common stock held by Xerox Corporation for approximately $80.0 million. In this transaction, Warburg Pincus acquired new warrants to purchase 2.5 million additional shar common stock for total consideration of $0.6 million. The warrants had a six-year life and an e $4.94 per share. In

NUANCE COMMUNICATIONS, INC.

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April 2010, the warrants to purchase 2.5 million shares of our common stock were exercised in cash proceeds to the Company of $12.4 million.

15. Stock-Based Compensation

We recognize stock-based compensation expense over the requisite service period. Our share-b accounted for as equity instruments. The amounts included in the consolidated statements of op to stock-based compensation are as follows (dollars in thousands):

	Three Months Ended June 30,		Nine M
	2010	2009	2010
Cost of product and licensing	$ 7	$ 2	$ 2
Cost of professional services and hosting	2,612	2,402	8,17
Cost of maintenance and support	165	132	58
Research and development	2,282	2,013	6,73
Sales and marketing	12,516	6,687	29,81
General and administrative	10,512	6,346	27,54
Total	$ 28,094	$ 17,582	$ 72,86

Stock Options

The table below summarizes activity relating to stock options for the nine months ended June 3

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	
Outstanding at September 30, 2009	13,553,866	$ 7.48		
Granted	1,200,000	$ 13.81		
Exercised	(3,235,920)	$ 5.36		
Forfeited	(331,559)	$ 13.62		
Expired	(99,788)	$ 15.87		
Outstanding at June 30, 2010	11,086,599	$ 8.52	3.7 years	$
Exercisable at June 30, 2010	8,021,090	$ 6.94	2.9 years	$

Exercisable at June 30, 2009	10,618,417	$	6.01	3.5 years	$

[1] The aggregate intrinsic value in this table was calculated based on the positive difference, the closing market value of our common stock on June 30, 2010 ($14.95) and the exercise underlying options.

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As of June 30, 2010, the total unamortized fair value of stock options was $14.6 million with a
average remaining recognition period of 0.9 years. A summary of weighted-average grant-date
stock options granted and intrinsic value of stock options exercised is as follows:

	Three Months Ended June 30,		Nine
	2010	2009	2010
Weighted-average grant-date fair value per share	n/a	$ 6.23	$ 5.90
Total intrinsic value of stock options exercised (in millions)	$ 7.1	$ 6.6	$ 34.1

We use the Black-Scholes option pricing model to calculate the grant-date fair value of an awa
of the stock options granted and unvested options assumed from acquisitions during the three a
ended June 30, 2010 and 2009 were calculated using the following weighted-average assumpti

	Three Months Ended June 30,		Nine
	2010	2009	2010
Dividend yield	n/a	0.0%	0.0%
Expected volatility	n/a	53.9%	50.9%
Average risk-free interest rate	n/a	2.5%	2.4%
Expected term (in years)	n/a	5.7	4.2

Restricted Units

Restricted Units are not included in issued and outstanding common stock until the shares are v
released. The table below summarizes activity relating to Restricted Units for the nine months
2010:

	Number of Shares Underlying Restricted Units Contingent Awards	Num U Res T
Outstanding at September 30, 2009	2,840,673	
Granted	1,519,243	
Earned/released	(918,015)	
Forfeited	(650,756)	

Outstanding at June 30, 2010		2,791,145	
Weighted average remaining contractual term of outstanding Restricted Units		1.0 years	
Aggregate intrinsic value of outstanding Restricted Units(1)	$	41.7 million	$
Restricted Units vested and expected to vest		2,467,305	
Weighted average remaining contractual term of Restricted Units vested and expected to vest		0.9 years	
Aggregate intrinsic value of Restricted Units vested and expected to vest(1)	$	36.9 million	$

(1) The aggregate intrinsic value in this table was calculated based on the positive difference closing market value of our common stock on June 30, 2010 ($14.95) and the exercise pri underlying Restricted Units.

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The purchase price for vested Restricted Units is $0.001 per share. As of June 30, 2010, unearn compensation expense related to all unvested Restricted Units is $119.0 million, which will, ba expectations of future performance vesting criteria, where applicable, be recognized over a wei period of 1.5 years.

A summary of weighted-average grant-date fair value, including those assumed in respective p intrinsic value of all Restricted Units vested is as follows:

	Three Months Ended June 30,		Nine M
	2010	2009	2010
Weighted-average grant-date fair value per share	$ 17.39	$ 12.30	$ 15.59
Total intrinsic value of shares vested (in millions)	$ 29.0	$ 5.5	$ 65.2

16. Income Taxes

The effective tax rate was 608.3% and 173.0% for the three months ended June 30, 2010 and 2 and (26.6)% and (263.1)% for the nine months ended June 30, 2010 and 2009, respectively. Inc provision for the three months ended June 30, 2010 was $2.7 million in foreign income tax pro by a $1.1 million discrete tax benefit resulting from the release of a contingency upon a favora settlement.

Included in the tax provision for the nine months ended June 30, 2010 was $8.1 million in fore provision, reduced by the release of a $1.1 million U.S. federal tax audit contingency discussed included was a $1.1 million tax benefit resulting from certain international research and develo credits, and a $1.0 million tax benefit resulting from the favorable settlement of a state tax pena acquisition of eScription. No tax benefit has been recognized for the U.S. losses in either the th month periods ended June 30, 2010 and 2009, as the realization of such tax benefit is not more

At June 30, 2010 and September 30, 2009, the liability for income taxes associated with uncert was $11.5 million and $12.1 million, respectively. The decrease is primarily attributable to the settlement of certain US tax contingencies. We do not expect a significant change in the amour unrecognized tax benefits within the next 12 months.

17. Commitments and Contingencies

Operating Leases

The following table outlines our gross future minimum payments under all non-cancelable ope June 30, 2010 (in thousands):

Year Ending September 30,	Operating Leases	Leases Under Restructuring	Other Contractua Obligation Assumed
2010 (July 1, 2010 to September 30, 2010)	$ 5,802	$ 1,019	$ 3,42
2011	20,908	3,287	13,94
2012	18,745	1,997	12,29
2013	16,943	901	2,32
2014	14,176		2,32
Thereafter	45,377		3,29
Total	$ 121,951	$ 7,204	$ 37,61

NUANCE COMMUNICATIONS, INC.

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At June 30, 2010, we have subleased certain office space that is included in the above table to t Total sublease income under contractual terms is $14.5 million and ranges from approximately $4.1 million on an annual basis through February 2016.

Litigation and Other Claims

Like many companies in the software industry, we have, from time to time, been notified of cla be infringing, or contributing to the infringement of, the intellectual property rights of others. T been referred to counsel, and they are in various stages of evaluation and negotiation. If it appe desirable, we may seek licenses for these intellectual property rights. There is no assurance tha offered by all claimants, that the terms of any offered licenses will be acceptable to us or that i dispute will be resolved without litigation, which may be time consuming and expensive, and r injunctive relief or the payment of damages by us.

Vianix LLC has filed three legal actions against us, consisting of two breach of contract action infringement claim. We believe that our maximum potential exposure, specifically related to o of contract actions and the copyright infringement claim, is immaterial. It is too early for us to conclusion as to the ultimate outcome or proposed settlement of these actions, or to estimate th that could result from a settlement or adverse judgment against us in the second breach of cont have not accrued any liability for these actions as we believe that we have substantial defenses claims, and intend to defend them vigorously.

We do not believe that the final outcome of the above litigation matters will have a material ad our financial position and results of operations. However, even if our defense is successful, the require significant management time and will be costly. Should we not prevail, our operating re position and cash flows could be adversely impacted.

Guarantees and Other

We include indemnification provisions in the contracts we enter into with customers and busin Generally, these provisions require us to defend claims arising out of our products infringeme intellectual property rights, breach of contractual obligations and/or unlawful or otherwise culp The indemnity obligations generally cover damages, costs and attorneys fees arising out of su but not all, cases, our total liability under such provisions is limited to either the value of the co specified, agreed upon amount. In some cases our total liability under such provisions is unlimi not all, cases, the term of the indemnity provision is perpetual. While the maximum potential a payments we could be required to make under all the indemnification provisions is unlimited, estimated fair value of these provisions is minimal due to the low frequency with which these p been triggered.

We indemnify our directors and officers to the fullest extent permitted by law. These agreemen things, indemnify directors and officers for expenses, judgments, fines, penalties and settlemen incurred by such persons in their capacity as a director or officer of the company, regardless of individual is serving in any such capacity at the time the liability or expense is incurred. Additi connection with certain acquisitions we have agreed to indemnify the former officers and mem boards of directors of those companies, on similar terms as described above, for a period of six acquisition date. In certain cases we purchase director and officer insurance policies related to which fully cover the six year periods. To the extent that we do not purchase a director and offi policy for the full period of any contractual indemnification, we would be required to pay for c any, as described above.

18. Segment and Geographic Information and Significant Customers

We follow the provisions of ASC 280 (formerly referred to as SFAS No. 131, *Disclosures Abo Enterprise and Related Information*), which establishes standards for reporting information abo segments. ASC 280 also established standards for disclosures about products, services and geo Operating segments are defined as components of an enterprise for which separate financial inf available and evaluated regularly by the chief operating decision maker in deciding how to allo and in assessing performance. Our chief operating decision maker (CODM) is the Chief Exe the Company.

We have several customer-facing market groups that oversee the core markets where we condu These groups are referred to as Mobile-Enterprise, Healthcare-Dictation, and Imaging. These g directly manage centralized or shared resources or the allocation decisions regarding the activit these functions, which include sales and sales operations, certain research and development ini development and all general and administrative activities. Our CODM oversees these groups a the functions that provide the shared and centralized activities noted above. To manage the bus resources and assess performance, the CODM primarily reviews revenue data by market group gross margins, operating margins, and other measures of income or loss on a consolidated basi determined that we operate in one segment.

The following table presents revenue information for our three core markets (in thousands):

	Three Months Ended June 30,		Nine M J
	2010	2009	2010
Mobile-Enterprise	$ 125,734	$ 118,056	$ 386,81
Healthcare-Dictation	125,087	105,575	363,52
Imaging	22,382	17,409	58,84
Total	$ 273,203	$ 241,040	$ 809,18

No country outside of the United States provided greater than 10% of our total revenue. Reven the major geographic areas in which our customers are located, was as follows (table in thousa

	Three Months Ended June 30,		Nine M J
	2010	2009	2010
United States	$ 202,080	$ 185,111	$ 576,12
International	71,123	55,929	233,06
Total	$ 273,203	$ 241,040	$ 809,18

No country outside of the United States held greater than 10% of our long-lived or total assets. assets, including intangible assets and goodwill, were located as follows (table in thousands):

	June 30, 2010
United States	$ 2,415,726
International	417,743
Total	$ 2,833,469

19. Related Parties

A member of our Board of Directors is also a partner at Wilson Sonsini Goodrich & Rosati, Pr Corporation, a law firm that provides professional services to us. These services may from time contingent fee arrangements. We paid Wilson Sonsini Goodrich & Rosati $0.3 million and $2.3 three and nine months ended June 30, 2010 for professional services. As of June 30, 2010 and S 2009, we had $2.0 million and $1.7 million, respectively, included in accounts payable and acc Wilson Sonsini Goodrich & Rosati.

Table of Contents

Item 2. *Management s Discussion and Analysis of Financial Condition and Results of Op*

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

FORWARD-LOOKING STATEMENTS

This Quarterly Report contains forward-looking statements, including predictions regarding:

our future revenue, cost of revenue, research and development expenses, selling, general administrative expenses, amortization of intangible assets and gross margin;

our strategy relating to our core markets;

the potential of future product releases;

our product development plans and investments in research and development;

future acquisitions, and anticipated benefits from pending and prior 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 expects, plans, anticipates, believes, estimates, predicts, intends, potentia terms, or other comparable terminology. Forward-looking statements also include the assumpti relating to any of the foregoing statements. Our actual results could differ materially from those these forward-looking statements for many reasons, including the risks described in Item 1A Part II and elsewhere in this Quarterly Report.

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

OVERVIEW

Nuance Communications, Inc. is a leading provider of speech, imaging and keypad solutions fo organizations and consumers around the world. Our technologies, applications and services ma experience more compelling by transforming the way people interact with devices and systems create, share and use documents. Our solutions are used every day by millions of people and th businesses for tasks and services such as requesting information from a phone-based self-servic dictating medical records, searching the mobile Web by voice, entering a destination into a nav or working with PDF documents. Our solutions help make these interactions, tasks and experie productive, compelling and efficient.

Our technologies address our three core markets:

Mobile-Enterprise. We deliver a portfolio of solutions that improve the experience of cu communications, mobile interactions and personal productivity. Combining our expertis and mobile solutions allows us to help consumers, businesses and manufacturers more e mobile devices for accessing an array of content, services and capabilities. Our enterpris automate a wide range of customer services and business processes in a variety of inforn process-intensive vertical markets such as telecommunications, financial services, utiliti entertainment, and government. Our mobile solutions add voice control and texting capa devices and services, allowing people to more easily dial a mobile phone, enter destinati into an automotive navigation system, dictate a text message or have emails and screen i aloud.

Healthcare-Dictation. Our healthcare solutions comprise a portfolio of speech-driven cl documentation and communication solutions that help healthcare provider organizations costs, increase reimbursement, and enhance patient care and safety. Our solutions autom management of medical information and are used by many of the largest hospitals in the We offer a variety of different solutions and deployment options to address the specific different healthcare provider organizations. Our Dragon NaturallySpeaking family of pr people and businesses increase productivity by using speech to create documents, stream and complex tasks, input data, complete forms and automate manual transcription proce Medical solution is a desktop application that provides front-end speech recognition that groups of physicians and clinicians to create and navigate medical records.

Imaging. Our PDF and document imaging solutions reduce the time and cost associated using and sharing documents. Our solutions benefit from the widespread adoption of the the increasing demand for networked solutions for managing electronic documents. Our used by millions of professionals and within large enterprises.

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

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

We have built a world-class portfolio of intellectual property, technologies, applications and so both internal development and acquisitions. We expect to continue to pursue opportunities to b assets and expand our customer base through acquisitions. In evaluating the financial condition performance of our business, management focuses on revenue, earnings, gross margins, operat cash flow from operations. A summary of these key financial metrics for the three-month perio 2010, as compared to the three-month period ended June 30, 2009, is as follows:

Total revenue increased by $32.2 million to $273.2 million;

Net loss decreased by $1.3 million to $1.5 million;

Gross profit increased by 1.7 percentage points to 62.7%;

Operating margins decreased to 1.7% from 7.1%; and

Cash provided by operating activities for the nine months ended June 30, 2010 was $184 increase of $0.4 million from the same period in the prior fiscal year.

CRITICAL ACCOUNTING POLICIES

Generally accepted accounting principles in the United States (GAAP) require us to make estir assumptions that affect the reported amounts of assets and liabilities and the disclosure of conti liabilities at the dates of the financial statements and the reported amounts of revenue and expe reporting periods. On an ongoing basis, we evaluate our estimates, assumptions and judgments related to: revenue recognition; allowance for doubtful accounts and returns; the costs to compl development of custom software applications; the valuation of goodwill, intangible assets and t long-lived assets; accounting for business combinations; share-based payments; valuation of de instruments; accounting for income taxes and related valuation allowances and loss contingenc management bases its estimates on historical experience, market participant fair value considerations and various other factors tha be reasonable under the circumstances. Actual results could differ from these estimates.

Information about those accounting policies we deem to be critical to our financial reporting m our Annual Report on Form 10-K for the fiscal year ended September 30, 2009. There have bee changes or additions to our critical accounting policies from those disclosed in our annual repo those changes in our policies for accounting for business combinations resulting from our adop [formerly referred to as Statement of Financial Accounting Standards (SFAS) No. 141(Revi *Combinations* (SFAS 141R)], as described in Note 2 to the unaudited consolidated financial in Item 1 of Part I of this Quarterly Report on Form 10-Q.

RECENTLY ISSUED ACCOUNTING STANDARDS

Refer to Note 2 to the unaudited consolidated financial statements included in Item 1 of Part I o Report on Form 10-Q.

RESULTS OF OPERATIONS

The following table presents, as a percentage of total revenue, certain selected financial data fo nine months ended June 30, 2010 and 2009 (as adjusted for the retrospective application of FA

	Three Months		Nin
	Ended June 30,		Ende
	2010	2009	2010
Revenue:			
Product and licensing	39.8%	36.3%	41.4
Professional services and hosting	43.2	46.0	41.8
Maintenance and support	17.0	17.7	16.8
Total revenue	100.0	100.0	100.0
Cost of revenue:			
Product and licensing	4.0	3.5	4.2
Professional services and hosting	26.1	28.3	25.5
Maintenance and support	2.8	3.0	2.9
Amortization of intangible assets	4.4	4.2	4.4
Gross profit	62.7	61.0	63.0
Operating expenses:			
Research and development	14.2	11.5	14.1
Sales and marketing	24.6	20.8	24.3
General and administrative	10.9	10.2	11.0
Amortization of intangible assets	7.9	8.3	8.1
Acquisition-related costs, net	2.2	1.9	3.3
Restructuring and other charges, net	1.2	1.2	2.0

Total operating expenses	61.0	53.9	62.8
Income from operations	1.7	7.1	0.2
Other income (expense), net	(1.6)	(5.5)	(2.3)
Income (loss) before income taxes	0.1	1.6	(2.1)
Provision for income taxes	0.7	2.7	0.5
Net loss	(0.6)%	(1.1)%	(2.6)

Total Revenue

The following tables show total revenue from our three core market groups and revenue by geo based on the location of our customers, in dollars and percentage change (dollars in millions):

	Three Months Ended June 30,		Dollar Change	Percent Change	Nine Months Ended June 30,		Do Ch
	2010	2009			2010	2009	
Mobile-Enterprise	$ 125.7	$ 118.0	$ 7.7	6.5%	$ 386.8	$ 332.4	$
Healthcare-Dictation	125.1	105.6	19.5	18.5	363.5	306.1	
Imaging	22.4	17.4	5.0	28.7	58.9	48.5	
Total Revenue	$ 273.2	$ 241.0	$ 32.2	13.4%	$ 809.2	$ 687.0	$
United States	$ 202.1	$ 185.1	$ 17.0	9.2%	$ 576.1	$ 519.6	$
International	71.1	55.9	15.2	27.2	233.1	167.4	
Total Revenue	$ 273.2	$ 241.0	$ 32.2	13.4%	$ 809.2	$ 687.0	$

The increase in total revenue for the three and nine months ended June 30, 2010, as compared t periods ended June 30, 2009, was driven by a combination of organic growth and contributions acquisitions. Mobile-Enterprise revenue increased primarily due to growth in sales of our predi products and embedded speech products for the automotive market, as well as contributions fro voicemail-to-text solutions. Healthcare-Dictation revenue increased primarily due to organic gr Dragon Medical and diagnostics products, iChart and eScription transcription services and Spe solutions. Imaging revenue increased primarily as a result of contributions from our acquisition and X-Solutions Group B.V and growth in our core imaging solutions.

Based on the location of our customers, the geographic split for the three and nine months ende was 74% and 71%, respectively, of total revenue in the United States and 26% and 29%, respec internationally. This represents a shift in revenues toward international as compared to 77% an revenue in the United States and 23% and 24% internationally for the same periods in fiscal 20 in the proportion of revenue generated internationally during the three and nine months ended J compared to the same periods in the prior year was primarily due to contributions from our acq SpinVox, as well as the increase in revenue contributions from our predictive text products and solutions, which are sold predominantly outside the United States.

Product and Licensing Revenue

Product and licensing revenue primarily consists of sales and licenses of our technology. The f shows product and licensing revenue, in dollars and as a percentage of total revenue (dollars in

	Three Months Ended	Nine Months Ended

	June 30,		Dollar	Percent	June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Product and licensing revenue	$ 108.8	$ 87.4	$ 21.4	24.5%	$ 335.2	$ 260.0	$
As a percentage of total revenue	39.8%	36.3%			41.4%	37.8%	

The increase in product and licensing revenue for the three months ended June 30, 2010, as cor
three months ended June 30, 2009, consisted of a $7.0 million increase in Mobile-Enterprise re
due to growth in sales of our predictive text products, as well as sales of our embedded speech
automotive market. Healthcare-Dictation revenue increased $10.7 million, primarily driven by
our Dragon Medical and diagnostics products and SpeechMagic solutions. Imaging revenue inc
$3.7 million primarily due to contributions from our acquisitions of eCopy and X-Solutions. Tl
product and licensing revenue streams outpaced the relative growth of our other revenue types,
3.5 percentage point increase as a percent of total revenue.

The increase in product and licensing revenue for the nine months ended June 30, 2010, as com months ended June 30, 2009, consisted of a $37.7 million increase in Mobile-Enterprise revenu to growth in sales of our predictive text products, as well as sales of our embedded speech prod automotive market. Healthcare-Dictation revenue increased $29.5 million primarily as a result of our SpeechMagic solutions and Dragon Medical products. Imaging revenue increased $8.0 r due to contributions from our acquisitions of X-Solutions and eCopy. The growth in our produ revenue streams outpaced the relative growth of our other revenue types, resulting in the 3.6 pe increase as a percent of total revenue.

Professional Services and Hosting Revenue

Professional services revenue primarily consists of consulting, implementation and training ser customers. Hosting revenue primarily relates to delivering hosted transcription and dictation se specified term, as well as self-service, on-demand offerings to carriers and enterprises. The foll shows professional services and hosting revenue, in dollars and as a percentage of total revenu millions):

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Professional services and hosting revenue	$ 117.9	$ 111.0	$ 6.9	6.2%	$ 337.8	$ 304.2	$
As a percentage of total revenue	43.2%	46.0%			41.8%	44.3%	

The increase in professional services and hosting revenue for the three months ended June 30, compared to the three months ended June 30, 2009, was driven by a $8.5 million increase in Healthcare-Dictation revenues resulting largely from growth of our iChart and eScription trans During the three months ended June 30, 2010, the annualized line run-rate in our healthcare on was approximately 3.242 billion lines per year, up 14% from 2.833 billion lines per year during months ended June 30, 2009. The annualized line run-rate is determined by the number of lines in a given quarter, multiplied by four. Mobile-Enterprise revenue decreased $1.7 million prima timing of revenue recognition related to enterprise set-up and implementation professional serv offset by contributions from our voicemail-to-text solutions. Our backlog hours in enterprise pr services were approximately 312,000 hours as of June 30, 2010, compared with approximately of June 30, 2009. Enterprise professional services backlog hours reflect the accumulated estima necessary to fulfill all of our existing, executed professional services contracts within the enter including those that are cancelable by customers, based on the original estimate of hours sold. of total revenue, professional services and hosting revenue decreased 2.8 percentage points as c corresponding period in the prior year, primarily due to the strong growth in product and licens relative to professional services and hosting revenue.

The increase in professional services and hosting revenue for the nine months ended June 30, 2 to the nine months ended June 30, 2009, was driven by a $24.3 million increase in Healthcare-l revenues resulting largely from growth of our iChart and eScription transcription services. Dur months ended June 30, 2010, the number of healthcare transcription lines processed increased a the corresponding period in the prior year. Mobile-Enterprise revenue increased $8.9 million, p contributions from our voicemail-to-text solutions and growth in our professional services for t markets. As a percentage of total revenue, professional services and hosting revenue decreased points as compared to the corresponding period in the prior year, primarily due to the strong gr and licensing revenue relative to professional services and hosting revenue.

Maintenance and Support Revenue

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

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Maintenance and support revenue	$ 46.5	$ 42.7	$ 3.8	8.9%	$ 136.2	$ 122.9	$
As a percentage of total revenue	17.0%	17.7%			16.8%	17.9%	

The increase in maintenance and support revenue for the three months ended June 30, 2010, as
three months ended June 30, 2009, consisted primarily of a $2.3 million increase in Mobile-En
driven by continued organic growth, and a $1.1 million increase in Imaging revenue primarily
contributions from our acquisition of X-Solutions and growth in sales of our core imaging prod

The increase in maintenance and support revenue for the nine months ended June 30, 2010, as
nine months ended June 30, 2009, consisted primarily of a $7.8 million increase in Mobile-Ent
driven by continued organic growth, and a $3.6 million increase related to the expansion of our
base of Healthcare-Dictation solutions.

COSTS AND EXPENSES

Cost of Product and Licensing Revenue

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

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Cost of product and licensing revenue	$ 10.9	$ 8.4	$ 2.5	29.8%	$ 34.2	$ 26.2	$
As a percentage of product and licensing revenue	10.0%	9.6%			10.2%	10.1%	

The increase in cost of product and licensing revenue for the three and nine months ended June compared to the same periods ended June 30, 2009, was primarily due to increased costs as a r our Healthcare-Dictation and Imaging product and licensing revenues. Gross margins relative t licensing revenue remained relatively constant across all periods presented.

Cost of Professional Services and Hosting Revenue

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

	Three Months Ended June 30,				Nine Months Ended June 30,		
	2010	2009	Dollar Change	Percent Change	2010	2009	D Cl
Cost of professional services and hosting revenue	$ 71.4	$ 68.3	$ 3.1	4.5%	$ 206.3	$ 189.6	$
As a percentage of professional services and hosting revenue	60.6%	61.5%			61.1%	62.3%	

The increase in cost of professional services and hosting revenue for the three months ended Ju compared to the three months ended June 30, 2009, was primarily due to increases in Mobile-E resulting from revenue growth in our voicemail-to-text solutions and revenue growth in our iC eScripiton transcription services.

The increase in cost of professional services and hosting revenue for the nine months ended Ju compared to the nine months ended June 30, 2009, was primarily due to increases in Mobile-E resulting primarily from revenue growth in our voicemail-to-text solutions.

Cost of Maintenance and Support Revenue

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

	Three Months Ended June 30,				Nine Months Ended June 30,		
	2010	2009	Dollar Change	Percent Change	2010	2009	D Cl
Cost of maintenance and support revenue	$ 7.6	$ 7.2	$ 0.4	5.6%	$ 23.3	$ 21.4	$
As a percentage of maintenance and support revenue	16.4%	16.9%			17.1%	17.4%	

Aggregate cost increases for the three and nine months ended June 30, 2010, as compared to th
periods in the prior year, were attributable to increases in our installed base of solutions. Gross
to our maintenance and support services remained relatively constant across all periods present

Research and Development Expense

Research and development expense primarily consists of salaries, benefits and overhead relatin
staff. The following table shows research and development expense, in dollars and as a percent
revenue (dollars in millions):

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Total research and development expense	$ 38.9	$ 27.7	$ 11.2	40.4%	$ 113.8	$ 85.6	$
As a percentage of total revenue	14.2%	11.5%			14.1%	12.5%	

The increase in research and development expense for the three months ended June 30, 2010, a
the three months ended June 30, 2009, was largely attributable to a $6.0 million increase in cor
expense from headcount growth in our core business as well as additional headcount from acqu
fiscal 2009 and 2010. In addition, there was a $4.2 million increase in research and developme
recorded for the three

months ended June 30, 2010 for services from a third party related to the collaboration agreem

The increase in research and development expense for the nine months ended June 30, 2010, as nine months ended June 30, 2009, was largely attributable to the $12.2 million in expense reco from a third party related to the collaboration agreements, as well as an $11.2 million increase expense from headcount growth in our core business as well as additional headcount from our during fiscal 2009 and 2010.

Sales and Marketing Expense

Sales and marketing expense includes salaries and benefits, commissions, advertising, direct m relations, tradeshow costs and other costs of marketing programs, travel expenses associated w organization and overhead. The following table shows sales and marketing expense, in dollars percentage of total revenue (dollars in millions):

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Total sales and marketing expense	$ 67.2	$ 50.2	$ 17.0	33.9%	$ 196.7	$ 160.9	$
As a percentage of total revenue	24.6%	20.8%			24.3%	23.4%	

The increase in sales and marketing expense for the three months ended June 30, 2010, as com months ended June 30, 2009, was primarily attributable to a $13.7 million increase in compens expenses, of which $5.8 million related to increased stock-based compensation. The remaining attributable to additional headcount from acquisitions and increased commission expense as a r revenue growth.

The increase in sales and marketing expense for the nine months ended June 30, 2010, as comp months ended June 30, 2009, was primarily attributable to a $32.0 million increase in compens expenses, of which $9.6 million related to increased stock-based compensation. The remaining attributable to additional headcount from acquisitions and increased commission expense as a r revenue growth.

General and Administrative Expense

General and administrative expense primarily consists of personnel costs for administration, fi resources, information systems, facilities and general management, fees for external profession including accountants and attorneys, insurance, and provisions for doubtful accounts. The follo general and administrative expense, in dollars and as a percentage of total revenue (dollars in m

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Do
	2010	2009	Change	Change	2010	2009	Ch
Total general and administrative expense	$ 29.9	$ 24.5	$ 5.4	22.0%	$ 88.6	$ 75.3	$
As a percentage of total revenue	10.9%	10.2%			11.0%	11.0%	

The increase in general and administrative expense for the three months ended June 30, 2010, a the three months ended June 30, 2009, was primarily attributable to increased stock-based com result of an overall increase in the Company s stock price during the period. As a percentage o general and administrative expense remained relatively constant.

The increase in general and administrative expense for the nine months ended June 30, 2010, a nine months ended June 30, 2009, was primarily attributable to increased stock-based compens of an overall increase in the Company s stock price during the period. As a percentage of total and administrative expense remained relatively constant.

Amortization of Intangible Assets

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

	Three Months Ended June 30,				Nine Months Ended June 30,		
	2010	2009	Dollar Change	Percent Change	2010	2009	D Ch
Cost of revenue	$ 11.9	$ 10.0	$ 1.9	19.0%	$ 35.1	$ 27.4	$
Operating expenses	21.5	19.9	1.6	8.0%	65.8	56.3	
Total amortization expense	$ 33.4	$ 29.9	$ 3.5	11.7%	$ 100.9	$ 83.7	$
As a percentage of total revenue	12.2%	12.4%			12.5%	12.2%	

The increase in amortization of intangible assets for the three and nine months ended June 30, compared to the three and nine months ended June 30, 2009, was primarily attributable to the a acquired intangible assets from our business acquisitions during fiscal 2009; our acquisition of the first quarter of fiscal 2010 and our acquisitions of patents and technology from other third- fiscal 2009 and fiscal 2010.

Acquisition-Related Costs, Net

Acquisition-related costs include those costs related to business and other acquisitions, includi acquisitions. These costs consist of transition and integration costs, including retention payme employee costs and earn-out payments treated as compensation expense, as well as the costs o integration-related services provided by third-parties; professional service fees, including direc of the transaction and post-acquisition legal and other professional service fees associated with regulatory matters related to acquired entities; and adjustments to acquisition-related items tha be marked to fair value each reporting period, such as contingent consideration, and other item acquisitions for which the measurement period has ended. Acquisition-related costs were reco (dollars in millions):

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,	
	2010	2009	Change	Change	2010	2009
Transition and integration costs	$ 3.4	$ 1.2	$ 2.2	183.3%	$ 12.1	$ 3.1
Professional service fees	3.1	3.4	(0.3)	(8.8)%	14.9	11.4
Acquisition-related adjustments	(0.4)	0.1	(0.5)	(500.0)%	(0.1)	(0.6)
Total Acquisition-related costs, net	$ 6.1	$ 4.7	$ 1.4	29.8%	$ 26.9	$ 13.9
As a percentage of total revenue	2.2%	1.9%			3.3%	2.0%

The increase in acquisition-related costs, net for the three months ended June 30, 2010, as com months ended June 30, 2009, was primarily attributable to increased transitional employee cost acquisitions of eCopy and SpinVox.

The increase in acquisition-related costs, net for the nine months ended June 30, 2010, as comp months ended June 30, 2009, was largely a result of our adoption on October 1, 2009 of the ne guidance relative to business combinations in FASB ASC 805. We recognized approximately $ transaction costs, included within professional service fees above, during the nine months ende that would have been capitalized in periods prior to our adoption of ASC 805, including approx $2.2 million that had been capitalized as of September 30, 2009 related to costs incurred in pri was required to be expensed upon our adoption of ASC 805. The remainder of the increase wa attributable to increased transitional employee costs from our acquisitions of eCopy and SpinV

Restructuring and Other Charges, Net

The following table sets forth the activity relating to the restructuring accruals for the nine mor June 30, 2010 (dollars in millions):

	Personnel	Facilities	Ot
Balance at September 30, 2009	$ 0.6	$ 0.3	$
Restructuring and other charges	8.2	0.2	
Non-cash adjustments			
Cash payments	(6.7)	(0.1)	
Balance at June 30, 2010	$ 2.1	$ 0.4	$

For the nine months ended June 30, 2010, we recorded net restructuring and other charges of $ which consisted primarily of $8.2 million related to the elimination of approximately 160 perso multiple functions within our company, including acquired entities, a $6.9 million write-off of capitalized patent defense costs as a result of unsuccessful litigation and $1.6 million of contra costs. Excluding the $6.9 million write-off of previously capitalized patent defense costs, restru have generally increased for the three and nine month periods ended June 30, 2010, as compare periods in the prior year, as a result of our current year adoption of the business combinations g ASC 805. Under the previous accounting guidance, restructuring costs related to acquired com generally recorded through purchase accounting, while the guidance in ASC 805 generally req costs be recorded to the acquiring company s statement of operations post-acquisition

Other Income (Expense), Net

The following table shows other income (expense), net in dollars and as a percentage of total re millions):

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		D
	2010	2009	Change	Change	2010	2009	Cl
Interest income	$ 0.2	$ 0.7	$ (0.5)	(71.4)%	$ 0.8	$ 3.2	$
Interest expense	(10.0)	(10.1)	0.1	1.0%	(30.4)	(36.8)	

Other income (expense), net	5.5	(3.8)	9.3	244.7%	10.7	2.0
Total other income (expense), net	$ (4.3)	$ (13.2)	$ 8.9	67.4%	$ (18.9)	$ (31.6)	$
As a percentage of total revenue	(1.6)%	(5.5)%			(2.3)%	(4.6)%

The gain of $5.5 million in other income (expense), net for the three months ended June 30, 20
driven by gains on foreign exchange as a result of the strengthening of the U.S. dollar and Briti
the Euro during the three months ended June 30, 2010. The loss of $3.8 million in other income
for the three months ended June 30, 2009, was primarily driven by losses in security price guar
derivatives as disclosed in Note 7 to the unaudited consolidated financial statements.

The gain of $10.7 million in other income (expense), net for the nine months ended June 30, 20 primarily driven by gains on foreign exchange as discussed above. The gain of $2.0 million in (expense), net for the nine months ended June 30, 2009, was primarily driven by gains in our n derivative instruments.

Provision for Income Taxes

The following table shows the provision for income taxes and the effective income tax rate (in dollars, except percentages):

	Three Months Ended June 30,		Dollar	Percent	Nine Months Ended June 30,		Doll
	2010	2009	Change	Change	2010	2009	Char
Income tax provision	$ 1.8	$ 6.7	$ (4.9)	(73.1)%	$ 4.5	$ 17.3	$ (1
Effective income tax rate	608.3%	173.0%			(26.6)%	(263.1)%	

Our effective income tax rate was 608.3% and 173.0% for the three months ended June 30, 201 respectively. The change in the effective tax rate primarily relates to the release of a U.S. tax co related to a favorable federal audit settlement during the three months ended June 30, 2010 and tax provision charge as a result of a Massachusetts state tax law enactment relating to the utiliz operating losses during the three months ended June 30, 2009. No tax benefit has been recogni U.S. losses, as the realization of such tax benefit is not more likely than not.

Our effective income tax rate was (26.6)% and (263.1)% for the nine months ended June 30, 20 respectively. The change in the effective tax rate primarily relates to an $8.0 million tax provis resulting from an asset purchase election made in 2009 in connection with the eScription acqui $3.2 million charge related to a state tax law enactment during 2009 as discussed above. No ta recognized for the U.S. losses, as the realization of such tax benefit is not more likely than not.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents totaled $492.1 million as of June 30, 2010, a decrease of $34.9 milli to $527.0 million as of September 30, 2009. Our working capital was $431.4 million as of June compared to $376.6 million as of September 30, 2009. As of June 30, 2010, our total accumula $283.5 million. We do not expect our accumulated deficit to impact our future ability to operat given our strong cash and operating cash flow positions, and believe our current cash and cash on-hand are sufficient to meet our operating needs for at least the next twelve months.

Cash Provided by Operating Activities

Cash provided by operating activities for the nine months ended June 30, 2010 was $184.7 mil
of $0.4 million, or 0.2%, as compared to cash provided by operating activities of $184.3 millio
months ended June 30, 2009. The increase was primarily driven by the following factors:

A decrease in cash of $60.7 million from accounts receivable primarily attributable to in
collection efforts and continuous DSO improvements during 2009, while maintaining co
receivable balances and DSO s in 2010;

An increase in cash resulting from a decrease in net loss, exclusive of non-cash adjustme
approximately $47.2 million;

An increase in cash of $36.2 million from deferred revenue primarily attributable to billi
imaging solutions; and

A decrease in cash from accounts payable and accrued expenses of $25.3 million primar
the timing of cash payments under our normal operating cycles.

Cash Used in Investing Activities

Cash used in investing activities for the nine months ended June 30, 2010 was $224.1 million, a $29.2 million, or 15%, as compared to cash used in investing activities of $194.9 million for th ended June 30, 2009. The net increase was primarily driven by the following factors:

A decrease of $50.4 million in cash payments for acquisitions of patents and technology

An increase of $42.0 million in cash payments related to business acquisitions, primaril cash paid in the acquisition of SpinVox, the PSRS deferred acquisition payment, and the earn-out payment;

An increase of $22.1 million in restricted cash related to cash placed in an irrevocable st credit account for a fixed obligation in connection with our acquisition of SpinVox; and

An increase of $14.8 million in cash payments for equity investments in a non-public co during the first quarter of 2010.

Cash Used in Financing Activities

Cash provided by financing activities for the nine months ended June 30, 2010 was $9.8 millio $157.8 million, or 94%, as compared to cash provided by financing activities of $167.6 million months ended June 30, 2009. The net decrease was primarily driven by the following factors:

A decrease of $162.8 million in cash from the sale of our common stock. During the nin June 30, 2009, we sold 17.4 million shares of our common stock and warrants to purcha shares of our common stock for net proceeds of $175.1 million;

An $11.8 million increase in cash from the exercise of company stock options and partic employee stock purchase plan; and

An $11.3 million decrease in cash resulting from greater cash paid to net share settle em awards, due to an increase in intrinsic value of the shares vested as a result of the overal stock price during the nine months ended June 30, 2010 as compared to the same period

2.75% Convertible Debentures

On August 13, 2007, we issued $250 million of 2.75% convertible senior debentures due in Au June 30, 2010, no conversion triggers were met. If the conversion triggers were met, we could repay all or some of the principal amount in cash prior to maturity.

Credit Facility

As of June 30, 2010, $645.2 million remained outstanding under our term loan. There were $1 letters of credit issued under the revolving credit line and there were no other outstanding borr revolving credit line. As of June 30, 2010, we are in compliance with the covenants under the

As of June 30, 2010, based on our leverage ratio, the applicable margin for our term loan was 1
rate borrowings and 2.00% for LIBOR-based borrowings. This results in an effective interest ra
payments under the excess cash flow sweep provision were due in the first quarter of fiscal 201
cash flow, as defined, was generated in fiscal 2009. At the current time, we are unable to predic
the outstanding principal, if any, that we may be required to repay in future fiscal years pursuan
cash flow

sweep provisions. If only the minimum required repayments are made, the annual aggregate pr
the term loans repaid would be as follows (table in thousands):

Year Ending September 30,
2010 (July 1, 2010 to September 30, 2010)
2011
2012
2013 (maturity)
Total

Equity

On March 19, 2004, we announced that Warburg Pincus had agreed to purchase all outstanding
warrants for our common stock held by Xerox Corporation for approximately $80.0 million. In
this transaction, Warburg Pincus acquired new warrants to purchase 2.5 million additional shar
common stock for total consideration of $0.6 million. The warrants had a six-year life and an e
$4.94 per share. In April 2010, the warrants to purchase 2.5 millions shares of our common sto
exercised in full, with total cash proceeds to the Company of $12.4 million.

We believe cash and cash equivalents on hand and cash flows from future operations will be su
our working capital and contractual obligations as they become due for the foreseeable future.
that in the event future operating results are not as planned, that we could take actions, includin
actions and other cost reduction initiatives, to reduce operating expenses to levels which, in co
expected future revenue, will continue to generate sufficient operating cash flow. In the event t
are not effective in generating operating cash flows, we may be required to issue equity or debt
terms that may be less than favorable.

Off-Balance Sheet Arrangements, Contractual Obligations

Contractual Obligations

The following table summarizes our outstanding contractual obligations as of June 30, 2010 (in

				Payments Due by Period	
				Fiscal	**Fisc**
		Remaining		**2012**	**201**
		Fiscal	**Fiscal**		
Contractual Obligations	**Total**	**2010**	**2011**	**and 2013**	**and 2**
2.75% Convertible Senior Debentures(1)	$ 250.0	$	$	$	$ 2.
Credit Facility(2)	645.3	1.7	6.7	636.9	
Interest on Credit Facility(2)	42.5	5.0	15.1	22.4	
	31.0	3.4	6.9	13.8	

Interest on 2.75% Convertible Senior Debentures(3)					
Lease obligations and other liabilities:					
Operating leases	122.0	5.8	20.9	35.7	
Other lease obligations associated with the closing of duplicate facilities related to restructurings and acquisitions	7.2	1.0	3.3	2.9	
Pension, minimum funding requirement	5.8	0.6	1.3	2.6	
Collaboration agreements(4)	83.6	18.4	20.9	41.8	
Other liabilities assumed(5)	37.6	3.4	13.9	14.6	
Total contractual cash obligations	$ 1,225.0	$ 39.3	$ 89.0	$ 770.7	$ 29

(1) Holders of 2.75% Convertible Senior Debentures can require us to repurchase the debentu
2014, 2017 and 2022.

(2) Interest is due and payable monthly, and principal is paid on a quarterly basis. The amoun
interest payable in this table are based on the effective interest rate as of March 31, 2010 e
effect of our interest rate swaps.

(3) These figures represent coupon interest only, payable by us in cash, semi-annually.

(4) Payments under the collaboration agreements are payable in cash or our common stock at

(5) Obligations include assumed long-term liabilities related to restructuring programs initiate
predecessor entities prior to our acquisition of SpeechWorks International, Inc. in August
acquisition of the former Nuance Communications, Inc. in September 2005. These restruc
relate to the closing of two facilities with lease terms set to expire in 2016 and 2012. Total
obligations under these two leases are $37.6 million. As of June 30, 2010, we have sub-lea
the office space related to these two facilities to unrelated third parties. Total sublease inco
remaining contractual terms is expected to be $14.5 million, which ranges from $1.5 milli
on an annualized basis through 2016.

Contingent Liabilities and Commitments

In connection with our acquisition of SNAPin Software, Inc. (SNAPin), we agreed to make
earn-out payment of up to $45.0 million in cash to be paid, if at all, based on the business achie
performance targets that are measurable from the acquisition date to December 31, 2009. In Ap
Company and the former shareholders of SNAPin agreed on a final earn-out payment of $21.2
issued 593,676 shares of our common stock, valued at $10.2 million, as our first payment unde
agreement. The remaining balance is payable in cash or stock, solely at our option, on or befor
and is included in long-term liabilities as of June 30, 2010.

In connection with our acquisition of Multi-Vision Communications, Inc. (Multi-Vision), w
contingent earn-out payments of up to $15.0 million, payable in stock, or cash, solely at our dis
to earn-out provisions described in the share purchase agreement. We have notified the former
Multi-Vision that the performance targets were not achieved. Through June 30, 2010, we have
obligation or related compensation expense relative to these measures.

In connection with our acquisition of Vocada, Inc. (Vocada), we agreed to make contingent
of up to $21.0 million, payable in stock, or cash, solely at our discretion, upon the achievement
financial targets measured over defined periods through December 31, 2010. Earn-out paymen
recorded as incremental purchase price and allocated to goodwill. We have notified the former
Vocada that the financial targets for certain periods were not achieved and they have requested
information regarding this determination. We are currently in discussions with the former share
Vocada regarding this matter. Through June 30, 2010, we have not recorded any earn-out oblig
the Vocada acquisition.

In connection with the acquisition of Commissure, Inc. (Commissure), we agreed to make c
payments of up to $8.0 million, payable in stock, or cash, solely at our discretion, upon the ach
certain financial targets for the fiscal years 2008, 2009 and 2010. Earn-out payments, if any, w

incremental purchase price and allocated to goodwill. We have notified the former shareholder
that the financial targets for the fiscal years 2008 and 2009 were not achieved and the related c
earn-out payment was not earned. Through June 30, 2010, we have not recorded any earn-out c
to the Commissure acquisition

Financial Instruments and Hedging Activities

We use financial instruments to manage our interest rate and foreign exchange risk. Financial A
Standards Board (FASB) Accounting Standards Codification (ASC) 815 (ASC 815), f
forward contracts and interest rate swaps.

To manage the interest rate exposure on our variable-rate borrowings, we use interest rate swap specific variable-rate debt into fixed-rate debt. As of June 30, 2010, we have two outstanding i designated as cash flow hedges with an aggregate notional amount of $200 million. The interes swaps are 2.7% and 2.1%, plus the applicable margin for the Credit Facility, and they expire in and November 2010, respectively. As of June 30, 2010 and September 30, 2009, the aggregate unrealized losses related to these swaps were $1.5 million and $4.0 million, respectively and w accumulated other comprehensive income (loss) in the accompanying balance sheets.

On October 1, 2009, we entered into foreign currency contracts to hedge exposure on the varia flows in Canadian dollars with a total notional amount of CAD$8.7 million. These contracts ar cash flow hedges. At June 30, 2010, one contract with unsettled notional amount of CAD $0.3 ($0.3 million based on the June 30, 2010 exchange rate) remained outstanding and was settled As of June 30, 2010, the aggregate cumulative unrealized gains related to these contracts were

In February and April 2010, we entered into foreign currency contracts to hedge exposure on t cash flows in Hungarian Forints (HUF) with a total notional amount of HUF 997.0 million. designated as cash flow hedges. At June 30, 2010, these contracts had an aggregate remaining, notional amount of HUF 403.0 million ($1.7 million based on the June 30, 2010 exchange rate settle monthly through December 2010. As of June 30, 2010, the aggregate cumulative unreali to these contracts were immaterial.

As of June 30, 2010, we have outstanding security price guarantees relative to a total of 1,785, common stock issued to a third party as discussed in Note 7 to the unaudited consolidated fina Changes in fair value of these security price guarantees are reported in earnings each period as income (expense) within other income (expense), net. For the three and nine months ended Ju recorded a decrease in fair value of $1.0 million and an increase in fair value of $3.7 million, r related to the settled and unsettled security price guarantees.

Off-Balance Sheet Arrangements

Through June 30, 2010, we have not entered into any off-balance sheet arrangements or materi with unconsolidated entities or other persons.

Item 3. *Quantitative and Qualitative Disclosures about Market Risk*

Our exposure to market risk has not changed materially from that disclosed in our Annual Rep for the fiscal year ended September 30, 2009.

Item 4. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures

Our management is responsible for establishing and maintaining a system of disclosure contro (as defined in Rule 13a-15 under the Securities Exchange Act of 1934 (the Exchange Act)) that information we are required to disclose in the reports that we file or submit under the Exch recorded, processed, summarized and reported within the time periods specified in the Securiti Commission s rules and forms. Disclosure controls and procedures include, without limitation procedures designed to ensure that information required to be disclosed by an issuer in the rep submits under the Exchange Act is accumulated and communicated to the issuer s manageme

principal executive officer or officers and principal financial officer or officers, or persons perf
functions, as appropriate to allow timely decisions regarding required disclosure.

We have evaluated the effectiveness of the design and operation of our disclosure controls and
the supervision of, and with the participation of, management, including our Chief Executive C
Financial Officer, as of the end of the period covered by this report. Based on that evaluation, c
Executive Officer and Chief Financial Officer have concluded that our disclosure controls and
effective to meet the requirements of Rule 13a-15 under the Exchange Act.

Changes in internal control over financial reporting

There were no changes to our internal controls over financial reporting identified in connection evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred du quarter covered by this Quarterly Report on Form 10-Q that have materially affected, or are rea materially affect, our internal control over financial reporting.

Part II. Other Information

Item 1. *Legal Proceedings*

This information is included in Note 17, Commitments and Contingencies, in the accompanyin consolidated financial statements and is incorporated herein by reference from Item 1 of Part I.

Item 1A. *Risk Factors*

You should carefully consider the risks described below when evaluating our company and wh whether to invest in our company. The risks and uncertainties described below are not the only Additional risks and uncertainties not presently known to us or that we do not currently believe an investor may also harm our business operations. If any of the events, contingencies, circum conditions described in the following risks actually occurs, our business, financial condition or operations could be seriously harmed. If that happens, the trading price of our common stock c 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 c decline.

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

- slowing sales by our distribution and fulfillment partners to their customers, which may these partners to reduce purchases of our products;

- volume, timing and fulfillment of customer orders;

- our efforts to generate additional revenue from our intellectual property portfolio;

- concentration of operations with one manufacturing partner and our inability to control e to the manufacturing, packaging and shipping of our boxed software products;

- customers delaying their purchasing decisions in anticipation of new versions of our pro

- customers delaying, canceling or limiting their purchases as a result of the threat or resul 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 c
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 collectibl

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 fo expense levels are based in significant part on our expectations of future revenue and we may r reduce our expenses quickly to respond to a shortfall in projected revenue. Therefore, our failu revenue expectations would seriously harm our operating results, financial condition and cash f

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

As part of our business strategy, we have in the past acquired, and expect to continue to acquir businesses and technologies. In connection with past acquisitions, we issued a substantial numb our common stock as transaction consideration and also incurred significant debt to finance the consideration used for our acquisitions. We may continue to issue equity securities for future a which would dilute existing stockholders, perhaps significantly depending on the terms of such may also incur additional debt in connection with future acquisitions, which, if available at all, additional restrictions on our ability to operate our business.

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

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

difficulty in transitioning and integrating the operations and personnel of the acquired bu

potential disruption of our ongoing business and distraction of management;

potential difficulty in successfully implementing, upgrading and deploying in a timely a manner new operational information systems and upgrades of our finance, accounting a distribution systems;

difficulty in incorporating acquired technology and rights into our products and technolo

potential difficulties in completing projects associated with in-process research and deve

unanticipated expenses and delays in completing acquired development projects and tec integration;

management of geographically remote business units both in the United States and inter

impairment of relationships with partners and customers;

assumption of unknown material liabilities of acquired companies;

accurate projection of revenue plans of the acquired entity in the due diligence process;

customers delaying purchases of our products pending resolution of product integration existing and our newly acquired products;

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 business
realize the anticipated benefits from our acquisitions. Any failure to achieve these benefits or fa
successfully integrate acquired businesses and technologies could seriously harm our business.

***Accounting treatment of our acquisitions could decrease our net income or expected revenu
foreseeable future, which could have a material and adverse effect on the market value of ou***

Under accounting principles generally accepted in the United States of America, we record the
our common stock or other form of consideration issued in connection with the acquisition and
which closed prior to October 1, 2009, the amount of direct transaction costs as the cost of acqu
company or business. We have allocated that cost to the individual assets acquired and liabiliti
including various identifiable intangible assets such as acquired technology, acquired tradenam
customer relationships based on their respective fair values. Intangible assets generally will be
five to ten year period. Goodwill and certain intangible assets with indefinite lives, are not subj
amortization but are subject to an impairment analysis, at least annually, which may result in a
charge if the carrying value exceeds its implied fair value. As of June 30, 2010, we had identifi
assets of approximately $667.9 million, net of accumulated amortization, and goodwill of appr
$2.0 billion. In addition, purchase accounting limits our ability to recognize certain revenue tha
would have been recognized by the acquired company as an independent business. The combi
delay revenue recognition or recognize less revenue than we and the acquired company would
as independent companies.

***Changes in the accounting method for business combinations may have an adverse impact o
or future financial results.***

For the years ended September 30, 2009 and prior, in accordance with Statement of Financial A
Standard (SFAS) 141 *Business Combinations,* (SFAS 141), all acquisition-related cos
and accountant s fees, as well as contingent consideration to the seller, which was recorded wh
reasonable doubt that the amount is payable, were capitalized as part of the purchase price.

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 14
Business Combinations, (SFAS 141R), now referred to as FASB Accounting Standards C
805), which requires an acquirer to do the following: expense acquisition-related costs as incu
payments as a reduction of cash flow from operations; record contingent consideration at fair v
acquisition date with subsequent changes in fair value to be recognized in the income statemen
from operations. ASC 805 applies to business combinations for which the acquisition date is o
October 1, 2009. ASC 805 could have a material impact on our results of operations and our fi
due to our acquisition strategy.

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

We have a significant amount of debt. As of June 30, 2010, we had a total of $897.1 million of
outstanding, including $645.2 million in term loans due in March 2013 and $250.0 million in c
debentures which investors may require us to redeem in August 2014. We also have a $75.0 mi
credit line available to us through March 2012. As of June 30, 2010, there were $15.9 million o
issued under the revolving credit line but there were no other outstanding borrowings under the
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, in convertible debentures and the credit facility, which will reduce the availability of our ca working capital, capital expenditures, acquisitions, research and development expenditu 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;

limit, along with the financial and other restrictive covenants in our debt, our ability to b
funds, dispose of assets or pay cash dividends.

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

In addition, a substantial portion of our debt bears interest at variable rates. If market interest ra
debt service requirements will increase, which would adversely affect our cash flows. While w
into interest rate swap agreements limiting our exposure for a portion of our debt, the agreemen
complete protection from this risk.

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

The agreement governing our senior credit facility contains, and any of our other future debt ag
contain, covenant restrictions that limit our ability to operate our business, including restriction
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
many factors, some of which are beyond our control, including prevailing economic conditions
these covenants, our ability to respond to changes in business and economic conditions and to o
financing, if needed, may be significantly restricted, and we may be prevented from engaging i
that might otherwise be beneficial to us. In addition, our failure to comply with these covenants
default under our debt agreements, which could permit the holders to accelerate our obligation
If any of our debt is accelerated, we may not have sufficient funds available to repay the accele

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

We reported net losses of $21.2 million for the nine months ended June 30, 2010 and $23.9 mil months ended June 30, 2009. If we are unable to achieve and maintain profitability, the market stock may decline, perhaps substantially. We cannot assure you that our revenue will grow or t achieve or maintain profitability in the future. If we do not achieve and maintain profitability, v required to raise additional capital to maintain or grow our operations. The terms of any transac additional capital, if available at all, may be highly dilutive to existing investors or contain othe terms, such as a high interest rate and restrictive covenants.

Speech technologies may not achieve widespread acceptance, which could limit our ability to speech business.

We have invested and expect to continue to invest heavily in the acquisition, development and speech technologies. The market for speech technologies is relatively new and rapidly evolving increase revenue in the future depends in large measure on the acceptance of speech technologi our products in particular. The continued development of the market for our current and future will also depend on:

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

Sales of our speech products would be harmed if the market for speech technologies does not c develop or develops slower than we expect, and, consequently, our business could be harmed a recover the costs associated with our investment in our speech technologies.

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

There are a number of companies that develop or may develop products that compete in our ta The individual markets in which we compete are highly competitive, and are rapidly changing. we compete with AT&T, Microsoft, Google, and other smaller providers. Within healthcare di transcription, we compete with Spheris, Medquist and other smaller providers. Within imaging directly with ABBYY, Adobe, I.R.I.S. and NewSoft. In speech, some of our partners such as A Edify, Genesys and Nortel develop and market products that can be considered substitutes for addition, a number of smaller companies in both speech and imaging produce technologies or in some markets competitive with our solutions. Current and potential competitors have establi establish, cooperative relationships among themselves or with third parties to increase the abili technologies to address the needs of our prospective customers.

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

Some of our customers, such as IBM, Microsoft and Google, have developed or acquired produ technologies that compete with our products and technologies. These customers may give high sale of these competitive products or technologies. To the extent they do so, market acceptance of our products, and therefore our revenue, may be adversely affected. Our success will depend upon our ability to enhance our products and technologies and to develop and introduce, on a ti cost-effective basis, new products and features that meet changing customer requirements and technological advancements. If we are unable to develop new products and enhance functional technologies to adapt to these changes, or if we are unable to realize synergies among our acqu technologies, our business will suffer.

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

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

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

Because we operate worldwide, our business is subject to risks associated with doing business We anticipate that revenue from international operations could increase in the future. Most of o revenue is generated by sales in Europe and Asia. In addition, some of our products are develop manufactured outside the United States and we have a large number of employees in India that transcription services. A significant portion of the development and manufacturing of our speec conducted in Belgium and Canada, and a significant portion of our imaging research and devel conducted in Hungary. We also have significant research and development resources in Aache Vienna, Austria. Accordingly, our future results could be harmed by a variety of factors associa 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 U 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 o States, we are exposed to the risk of changes in foreign currency exchange rates or declining ec conditions in these countries. In certain circumstances, we have entered into forward exchange hedge against foreign currency fluctuations. We use these contracts to reduce our risk associate rate movements, as the gains or losses on these contracts are intended to offset any exchange ra on the hedged transaction. We do not engage in foreign currency speculation. Forward exchang hedging firm commitments qualify for hedge accounting when they are designated as a hedge o currency exposure and they are effective in minimizing such exposure. With our increased inte presence in a number of geographic locations and with international revenue and costs projecte are exposed to changes in foreign currencies including the Euro, British Pound, Canadian Doll Indian Rupee and the Hungarian Forint. Changes in the value of the Euro or other foreign curre 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 future operating results.

We have significant intangible assets, including goodwill and intangibles with indefinite lives, susceptible to valuation adjustments as a result of changes in various factors or conditions. The intangible assets are patents and core technology, completed technology, customer relationship

Customer relationships are amortized on an accelerated basis based upon the pattern in which t benefits of customer relationships are being utilized. Other identifiable intangible assets are am straight-line basis over their estimated useful lives. We assess the potential impairment of ident assets on an annual basis, as well as whenever events or changes in circumstances indicate that value may not be recoverable. Factors that could trigger an impairment of such assets, include t

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

significant negative industry or economic trends;

significant decline in our stock price for a sustained period;

changes in our organization or management reporting structure could result in additional which may require alternative methods of estimating fair values or greater disaggregatio 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 ch 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, inves sanctions and penalties.

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

We conducted an analysis of our compliance with the terms and conditions of certain contracts U.S. General Services Administration (GSA). Based upon our analysis, we voluntarily notif non-compliance with the terms of two contracts. The final resolution of this matter may advers 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 qualifi could experience a loss in productivity while any successor obtains the necessary training and e employment relationships are generally at-will and we have had key employees leave in the pa assure you that one or more key employees will not leave in the future. We intend to continue t highly qualified personnel, including software engineers and operational personnel, but may no attract, assimilate or retain qualified personnel in the future. Any failure to attract, integrate, m these employees could harm our business.

Our medical transcription services may be subject to legal claims for failure to comply with l the confidentiality of medical records.

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

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 propo Care Financing Administration.

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

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

As our business has grown, we have become increasingly subject to the risks arising from adve domestic and global economic and political conditions. For example, the direction and relative U.S. and global economies have recently been increasingly uncertain due to softness in housing extreme volatility in security prices, severely diminished liquidity and credit availability, rating certain investments and declining valuations of others and continuing geopolitical uncertainties growth in the United States and other countries in which we do business is slowed, customers r reduce technology purchases and may be unable to obtain credit to finance the purchase of our could result in reduced sales of our products, longer sales cycles, slower adoption of new techn increased price competition. Any of these events would likely harm our business, results of ope financial condition. Political instability in any of the major countries in which we do business harm our business, results of operations and financial condition.

Current uncertainty in the global financial markets and the global economy may negatively financial results.

Current uncertainty in the global financial markets and economy may negatively affect our fina These macroeconomic developments could negatively affect our business, operating results or condition in a number of ways which, in turn, could adversely affect our stock price. A prolong economic decline could have a material adverse effect on our results of operations and financia exacerbate some of the other risk factors described herein. Our customers may defer purchases licenses, and services in response to tighter credit and negative financial news or reduce their d Our customers may also not be able to obtain adequate access to credit, which could affect thei timely payments to us or ultimately cause the customer to file for protection from creditors und insolvency or bankruptcy laws. If our customers are not able to make timely payments to us, ou receivable could increase.

Our investment portfolio, which includes short-term debt securities, is generally subject to cred counterparty, market and interest rate risks that may be exacerbated by the recent global financ banking system or the fixed income, credit or equity markets deteriorate or remain volatile, our portfolio may be impacted and the values and liquidity of our investments could be adversely a

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

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

our financial counterparties or other contractual counterparties are unable to, or do not, r
contractual commitments to us.

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

The uninterrupted operation of our hosted solutions and the confidentiality and security of thirc information is critical to our business. Any failures in our security and privacy measures could adverse effect on our financial position and results of operations. If we are unable to protect, or perceive that we are unable to protect, the security and privacy of our electronic information, o 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 proces transactions, there can be no assurance that our use of these applications will be sufficient to ac market conditions or the security and privacy concerns of existing and potential clients.

Risks Related to Our Intellectual Property and Technology

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

Our success and competitive position depend in large part on our ability to obtain and maintain property rights protecting our products and services. We rely on a combination of patents, copy trademarks, service marks, trade secrets, confidentiality provisions and licensing arrangements protect our intellectual property and proprietary rights. Unauthorized parties may attempt to co products or to obtain, license, sell or otherwise use information that we regard as proprietary. P unauthorized use of our products is difficult and we may not be able to protect our technology unauthorized use. Additionally, our competitors may independently develop technologies that a the same or superior to our technologies and that do not infringe our rights. In these cases, we to prevent our competitors from selling or licensing these similar or superior technologies. In a of some foreign countries do not protect our proprietary rights to the same extent as the laws of States. Although the source code for our proprietary software is protected both as a trade secret copyrighted work, litigation may be necessary to enforce our intellectual property rights, to pro secrets, to determine the validity and scope of the proprietary rights of others, or to defend agai infringement or invalidity. Litigation, regardless of the outcome, can be very expensive and car management efforts.

Third parties have claimed and may claim in the future that we are infringing their intellectu we could be exposed to significant litigation or licensing expenses or be prevented from sellir if such claims are successful.

From time to time, we are subject to claims that we or our customers may be infringing or cont infringement of the intellectual property rights of others. We may be unaware of intellectual pr others that may cover some of our technologies and products. If it appears necessary or desirab licenses for these intellectual property rights. However, we may not be able to obtain licenses f claimants, the terms of any offered licenses may not be acceptable to us, and we may not be ab disputes without litigation. Any litigation regarding intellectual property could be costly and ti and could divert the attention of our management and key personnel from our business operatio of a claim of intellectual property infringement, we may be required to enter into costly royalty agreements. Third parties claiming intellectual property infringement may be able to obtain inj equitable relief that could effectively block our ability to develop and sell our products.

Table of Contents

We may incur substantial costs enforcing or acquiring intellectual property rights and defen 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 th intellectual property rights, or disputes relating to the validity or alleged infringement of third-p property rights, including patent rights, we have been, are currently, and may in the future be, s negotiations or complex, protracted litigation. Intellectual property disputes and litigation are ty costly and can be disruptive to our business operations by diverting the attention and energy of key technical personnel. Although we have successfully defended or resolved past litigation an may not prevail in any ongoing or future litigation and disputes. In addition, we may incur sign acquiring the necessary third party intellectual property rights for use in our products. Third pa property disputes could subject us to significant liabilities, require us to enter into royalty and l arrangements on unfavorable terms, prevent us from manufacturing or licensing certain of our severe disruptions to our operations or the markets in which we compete, or require us to satisf commitments with our customers including contractual provisions under various license arrang these could seriously harm our business.

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

Complex software products such as ours may contain errors, defects or bugs. Defects in the sol products that we develop and sell to our customers could require expensive corrections and res lost revenue, adverse customer reaction and negative publicity about us or our products and ser who are not satisfied with any of our products may also bring claims against us for damages, w unsuccessful, would likely be time-consuming to defend, and could result in costly litigation ar 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 stockho

As of June 30, 2010, Warburg Pincus beneficially owned approximately 24% of our outstandin including warrants exercisable for up to 7,562,422 shares of our common stock, and 3,562,238 outstanding Series B Preferred Stock, each of which is convertible into one share of our comm of its large holdings of our capital stock relative to other stockholders, this stockholder has a st over matters requiring approval by our stockholders.

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

Our stock price historically has been, and may continue to be, volatile. Various factors contribu volatility of the stock price, including, for example, quarterly variations in our financial results introductions by us or our competitors and general economic and market conditions. Sales of a number of shares of our common stock by our largest stockholder, or the perception that such s could also contribute to the volatility or our stock price. While we cannot predict the individual factors may have on the market price of our common stock, these factors, either individually or could result in significant volatility in our stock price during any given period of time. Moreove that have experienced volatility in the market price of their stock often are subject to securities litigation. If we were the subject of such litigation, it could result in substantial costs and divert attention and resources.

Compliance with changing regulation of corporate governance and public disclosure may re expenses.

Changing laws, regulations and standards relating to corporate governance and public disclosu Sarbanes-Oxley Act of 2002, new regulations promulgated by the Securities and Exchange Co rules of The Nasdaq Global Select Market, are resulting in increased general and administrativ companies such as ours. These new or changed laws, regulations and standards are subject to v interpretations in many cases, and as a result, their application in practice may evolve over tim guidance is provided by regulatory and governing bodies, which could result in higher costs ne ongoing revisions to disclosure and governance practices. We are committed to maintaining hi corporate governance and public disclosure. As a result, we intend to invest resources to compl laws, regulations and standards, and this investment may result in increased general and admin and a diversion of management time and attention from revenue-generating activities to compl our efforts to comply with new or changed laws, regulations and standards differ from the activ regulatory or governing bodies, our business may be harmed.

Future sales of our common stock in the public market could adversely affect the trading pri 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 perceptio could occur, could adversely affect prevailing trading prices of our common stock and could in to raise capital through future offerings of equity or equity-related securities. In connection wit acquisitions, we issued a substantial number of shares of our common stock as transaction con may continue to issue equity securities for future acquisitions, which would dilute existing stoc perhaps significantly depending on the terms of such acquisitions. For example, we issued, and resale, approximately 2.3 million shares of our common stock in connection with our Decembe acquisition of SpinVox. No prediction can be made as to the effect, if any, that future sales of s stock, or the availability of shares of common stock for future sale, will have on the trading pri common stock.

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

Provisions of our certificate of incorporation, bylaws and Delaware law, as well as other organ documents could make it more difficult for a third party to acquire us, even if doing so would b 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 stockhold

Item 2. ***Unregistered Sales of Equity Securities and Use of Proceeds***

On April 30, 2010, we issued 593,676 shares of our common stock to former shareholders of S
payment of the earn-out portion of the merger consideration. The shares were issued in relianc
exemption from the registration requirements of the Securities Act of 1933, as amended, provi
Section 4(2) thereof because the issuance did not involve a public offering.

On May 20, 2010, we issued 237,499 shares of our common stock to the shareholders of Shap
partial consideration for our acquisition of Shapewriter, Inc. The shares were issued in relianc
exemption from the registration requirements of the Securities Act of 1933, as amended, provi
Section 4(2) thereof because the issuance did not involve a public offering.

On May 26, 2010, we issued a total of 20,450 shares of our common stock to Pagemill Partners payment for services in connection with our acquisition of Language and Computing, Inc. The issued in reliance upon an exemption from the registration requirements of the Securities Act o amended, provided by Section 4(2) thereof because the issuance did not involve a public offeri

On June 25, 2010, we issued 152,440 shares of our common stock to International Business Ma Corporation as consideration for a collaboration agreement. The shares were issued in reliance exemption from the registration requirements of the Securities Act of 1933, as amended, provic Section 4(2) thereof because the issuance did not involve a public offering.

Item 3. *Defaults Upon Senior Securities*

None.

Item 5. *Other Information*

None.

Item 6. *Exhibits*

The exhibits listed on the Exhibit Index are filed or incorporated by reference (as stated therein Quarterly Report on Form 10-Q.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly ca
Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly a
Town of Burlington, Commonwealth of Massachusetts, on August 9, 2010.

Nuance Communications, Inc.

By: /s/ Thomas L. Beaudoin

Thomas L. Beaudoin
Executive Vice President and Chief Financial Officer

EXHIBIT INDEX

		Incorporated by Referen			
Exhibit					Filin
Number	Exhibit Description	Form	File No.	Exhibit	Dat
3.1	Amended and Restated Certificate of Incorporation of the Registrant.	10-Q	0-27038	3.2	5/11/2
3.2	Certificate of Amendment of the Amended and Restated Certificate of Incorporation of the Registrant.	10-Q	0-27038	3.1	8/9/20
3.3	Certificate of Ownership and Merger.	8-K	0-27038	3.1	10/19/2
3.4	Certificate of Amendment of the Amended and Restated Certificate of Incorporation of the Registrant.	S-8	333-142182	3.3	4/18/2
3.5	Amended and Restated Bylaws of the Registrant.	10-K	0-27038	3.2	3/15/2
10.1*	Letter, dated March 29, 2010, to Janet Dillione regarding certain employment matters.				
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) or 15d-14(a).				
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) or 15d-14(a).				
32.1	Certification Pursuant to 18 U.S.C. Section 1350.				
101	The following materials from Nuance Communications, Inc. s Quarterly Report on Form 10-Q for the quarter ended June 30, 2010, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Balance Sheets, (iii) the Consolidated Statements of Cash Flows, and (iv) Notes of Consolidated Financial Statements.				

* Denotes management compensatory plan or arrangement