

SONIC FOUNDRY INC
Form 10-K
November 22, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal period ended September 30, 2010

OR

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

Commission File Number 000-30407

SONIC FOUNDRY, INC.

(Exact name of registrant as specified in its charter)

MARYLAND
(State or other jurisdiction of
incorporation or organization)

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

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

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

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

None

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

Common stock par value \$0.01 per share

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

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

The aggregate market value of the registrant's common stock held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the Registrant's most recently completed second fiscal quarter was approximately \$23,566,000.

The number of shares outstanding of the registrant's common equity was 3,641,107 as of November 18, 2010.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2010 Annual Meeting of Stockholders are incorporated by reference into Part III. A definitive Proxy Statement pursuant to Regulation 14A will be filed with the Commission no later than January 28, 2011.

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Explanatory Note:	

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

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For the Year Ended September 30, 2010

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

PART I

ITEM 1. BUSINESS

Who We Are

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

Sonic Foundry solutions include:

Mediasite Recorders for capturing multimedia presentations

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

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

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

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

Today, nearly 2,000 customers using more than 4,500 Mediasite Recorders in presentation venues around the world are capturing hundreds of thousands of multimedia presentations with millions of viewers.

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

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Challenges We Address

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

Ensuring students' academic and professional success

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

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

Helping students balance education, career and family commitments

Increasing enrollment without the expense of new classrooms and facilities

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

Simultaneously addressing people in multiple locations

Holding meetings, conferences and events when it is not feasible for everyone to attend

Transmitting timely information that is crucial for all to receive

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

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

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Maintaining productivity while in training

Reducing time to train new hires

Increasing retention by avoiding distractions, interruptions or absence

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

Documenting meeting content for later review

Extending the life of annual conferences and regional meetings

Maintaining a rich library of organizational knowledge

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

Cutting travel expenses and carbon footprints

Eliminating repetition of the same presentation to different audiences

Reducing repeated costs for printing, mailing and meeting expenses

Enabling individuals to attend professional conferences in light of travel bans and budget cuts
Avoiding cumbersome and restrictive technologies

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

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

Removing significant time and specialized expertise to manage presentation systems
Sonic Foundry Solutions

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

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Mediasite Recorders for capturing multimedia presentations

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

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

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

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

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Mediasite Recorders are designed with presenters in mind. They automatically record what presenters say and show, without changing how they present, and webcast it online. Mediasite Recorders streamline the capture and delivery of any presenters' video and any presentation images shown from any presentation source such as a laptop, tablet PC, document camera, whiteboard or even medical instrumentation. The result is high resolution, interactive presentations that can be immediately watched via the web—live or on-demand. With the industry's simplest workflow, Mediasite Recorders eliminate time-consuming authoring, slide uploads and post-production work. Plus, seamless integration with existing audio/video and educational technology means organizations can confidently scale multimedia webcasting throughout their academic or corporate enterprise.

We offer Mediasite Recorders for the following environments:

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

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

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

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

Mediasite EX Server allows organizations to:

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

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

Secure presentations and Mediasite system access for authorized users

Customize and brand their presentation content

Incorporate audience interactivity through polls and Q&A

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

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

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

Integrate Mediasite content into other course/learning/content management systems, portals, blogs or online communities

Leverage existing network technologies for content distribution efficiency and performance

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

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

Enhances attendee experience with online presentation catalogs

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

Brands presentations using organization logos, colors and messages

Provides a real-time record of what took place

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

Offers sample content to entice new attendees to participate

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

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

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

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

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

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

Software upgrades and updates for Mediasite Recorders and Servers

Unlimited technical support assistance

Extension of their recorder hardware warranty

Advanced recorder hardware replacement

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

Nearly all our customers purchase a Customer Assurance plan when they purchase Mediasite Recorders or Servers.

What Sets Mediasite Apart?

Market Leadership Two leading industry analyst firms recognize Sonic Foundry's Mediasite as the leading, best-of-breed platform for lecture capture. Frost & Sullivan awarded Sonic Foundry three consecutive Market Share Leadership Awards for Lecture Capture in 2010, 2009 and 2007 (no report was published in 2008). The Frost & Sullivan Award for Market Share Leadership is presented to the company that demonstrates excellence in capturing the highest market share within its industry and recognizes the company's leadership position in terms of revenues or units. Wainhouse Research also recognizes Mediasite as a streaming and lecture capture market leader for distance education and e-learning in their report, *The Distance Education and e-Learning Landscape V2* (December 2008). Among Wainhouse's evaluation criteria are innovation, market understanding, overall viability, product strategy and customer experience. According to the report, Sonic Foundry ranks highest from the perspective of product offering depth and ranks among the leaders in its ability to execute.

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

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

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Reliability Whether starting at the department level with a couple rooms or at the enterprise level with a campus- or company-wide implementation, Mediasite was developed to be the single platform to confidently and reliably scale to organizations' webcasting needs. Nearly 2,000 customers around the world depend on Mediasite and its proven design to webcast critical information, enrich daily communications and retain their organizational knowledge.

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

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

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

Sonic Foundry Solutions in Higher Education and the Enterprise

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

Sonic Foundry solutions in higher education:

Among post-secondary institutions, Mediasite is used for:

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

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Distance learning: off-campus students learn remotely online

Continuing education: professionals learn online or supplement classroom experiences

Faculty training and development

Research and collaboration: faculty document and present findings

Recruitment and orientation: campus tours, financial aid instructions

Special events: commencement, guest speakers, sporting events

University business: leadership meetings, alumni relations, outreach

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Through interviews, many higher education institutions report that Mediasite:

Improves student learning outcomes

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

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

Contributes to enhanced grades

Caters to different learning modalities

Enables their institution to remain competitive

Allows quick development and delivery of cost-effective online programs

Supports higher enrollment and/or tuition without new classrooms

Improves student retention and matriculation

Helps attract students and faculty

Empowers faculty

Allows them to teach as usual without learning new technology

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

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Improves student outcomes

Enables knowledge sharing and collaboration with colleagues

Supports time-shifting, letting faculty travel to conferences or present findings without missing class

Boosts campus outreach

Bolsters recruitment efforts

Increases awareness and reach of campus events

Enhances alumni relations

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

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

According to the Sloan Consortium report, *Learning on Demand: Online Education in the United States, 2009*, online enrollments the past several years have been growing considerably. The 17 percent growth rate for online enrollments far exceeds the 1.2 percent growth of the overall higher education student population. In the 2008 fall term, over 4.6 million, or more than one in four college and university students, were taking at least one online course, a 17 percent increase over the previous year. The economic downturn has also increased demand for online courses, with 66 percent of institutions reporting increased demand for new courses and programs, and 73 percent seeing increased demand for existing online courses and programs. Of public institutions, 74 percent believe that online education is critical for their long-term strategy, along with half of private for-profit and private nonprofit institutions.

Community colleges, specifically, have significantly increased their number of blended or hybrid and web-enhanced courses. The Instructional Technology Council's 2009 Distance Education Survey Results: *Trends in eLearning: Tracking the Impact of eLearning at Community Colleges* (March 2010) reported a 22 percent increase for distance learning enrollments, substantially higher than overall national campus enrollments, which averaged less than two percent nationally. The study also showed that overall, 74 percent of community colleges offer audio/video streaming, and another 15 percent plan to offer over the next two years. Over half of community colleges plan to increase the number of blended/hybrid courses.

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According to the 2009 *Campus Computing* survey, more than half of all universities already have a strategic plan for lecture capture or are working on one. And analysts predict the lecture capture market will more than triple over the next six years. Frost & Sullivan analysts estimate lecture capture revenues will reach over \$192 million by 2016, exhibiting a nearly 22 percent compound annual growth rate (CAGR) for the six-year period (*World Lecture Capture Solutions Markets* report, 2010).

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

Several universities have conducted their own independent studies to assess the impact of Mediasite on student performance. Penn State Hershey Medical Center and College of Medicine, a Mediasite campus since January 2004, deployed a pilot program at the onset of the 2007-2008 academic year to record lectures to first year medical students. During this academic year, lectures were viewed a total of 22,451 times, averaging 59.1 views per lecture by a class of 154 students. Mediasite use increased throughout the academic year, with 97 percent of students using Mediasite to review lectures by the semester's end. Almost half of the students surveyed (41 percent) cited reviewing complicated material as the number one motivator for using Mediasite. The majority (88 percent) agreed that Mediasite helps them achieve their educational goals. Much fewer (25 percent) said podcasting had the same effect. Faculty members reported that recording their lectures did not decrease class attendance. The survey also revealed a correlation between the grading method and the use of Mediasite. Students watch lectures more often via Mediasite for classes where grades are awarded as honors, high pass, pass and fail versus simply pass/fail.

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

During the spring semester of 2008, the University of New Mexico surveyed almost a thousand undergraduate and distance education students about their Mediasite usage and found:

90 percent of respondents agreed or strongly agreed that Mediasite should be available for other courses

62 percent of students used Mediasite at least half of the time or more to review or watch lectures

77 percent had good or excellent experiences using Mediasite, and 77 percent of respondents agreed or strongly agreed that Mediasite was easy to use

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85 percent described the quality of the Mediasite recordings as good or excellent

42 percent used Mediasite to review lec