OMNICELL, Inc
Form 10-Q
May 12, 2014
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2014

OR

o 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 000-33043

Omnicell, Inc.
(Exact name of registrant as specified in its charter)

Delaware	94-3166458
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

590 East Middlefield Rd.
Mountain View, CA 94043
(650) 251-6100
(Address, including zip code, of registrant's principal executive offices and registrant's telephone number, including area code)

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 o

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 x No o

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 o	Accelerated filer x

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

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

The number of shares of Registrant's common stock (par value $0.001) outstanding as of May 2, 2014 was 36,605,717.

Table of Contents
OMNICELL, INC.

FORM 10-Q

Table of Contents

Table of Contents

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

OMNICELL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited, in thousands)

	March 31, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$107,558	$ 104,531
Accounts receivable, net of allowances of $710 and $490, respectively	75,496	58,597
Inventories	30,975	31,457
Prepaid expenses	16,378	18,883
Deferred tax assets	12,636	12,635
Other current assets	7,799	7,675
Total current assets	250,842	233,778
Property and equipment, net	35,178	35,254
Non-current net investment in sales-type leases	11,644	11,485
Goodwill	111,343	111,343
Intangible assets, net	80,573	81,602
Non-current deferred tax assets	1,164	1,102
Other assets	19,661	17,937
Total assets	$510,405	$ 492,501
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$20,154	$ 16,471
Accrued compensation	12,018	19,604
Accrued liabilities	13,494	13,746
Deferred service revenue	21,328	22,626
Deferred gross profit	25,106	19,957
Total current liabilities	92,100	92,404
Non-current deferred service revenue	19,773	17,763
Non-current deferred tax liabilities	27,926	28,162
Other long-term liabilities	5,430	5,175
Commitments and Contingencies (Note 10 and Note 11)		
Total liabilities	145,229	143,504
Stockholders' equity:		
Total stockholders' equity	365,176	348,997
Total liabilities and stockholders' equity	$510,405	$ 492,501

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

OMNICELL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited, in thousands, except per share data)

	Three Months Ended March 31,	
	2014	2013
Revenues:		
Product revenues	$82,580	$69,236
Services and other revenues	19,184	17,874
Total revenues	101,764	87,110
Cost of revenues:		
Cost of product revenues	38,900	33,547
Cost of services and other revenues	8,369	8,196
Total cost of revenues	47,269	41,743
Gross profit	54,495	45,367
Operating expenses:		
Research and development	6,121	7,954
Selling, general and administrative	38,420	33,244
Total operating expenses	44,541	41,198
Income from operations	9,954	4,169
Interest and other income (expense), net	(256)	(223)
Income before provision for income taxes	9,698	3,946
Provision for income taxes	3,504	561
Net income	$6,194	$3,385
Net income per share-basic	$0.18	$0.10
Net income per share-diluted	$0.17	$0.10
Weighted average shares outstanding:		
Basic	35,225	33,900
Diluted	36,305	34,820

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

OMNICELL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited, in thousands)

	Three Months Ended March 31,	
	2014	2013
Net income	$6,194	$3,385
Other comprehensive income:		
Changes in fair value of foreign currency forward hedges	—	(65)
Foreign currency translation adjustment	33	(203)
Other comprehensive income (loss)	33	(268)
Comprehensive income	$6,227	$3,117

The accompanying notes are an integral part of these condensed consolidated financial statements

Table of Contents

OMNICELL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Three Months Ended March 31,	
	2014	2013
Cash flows from operating activities:		
Net income	$6,194	$3,385
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,612	4,472
Loss on disposal of fixed assets	191	41
Impairment of software development costs	—	1,759
Provision for receivable allowance	217	129
Share-based compensation expense	2,729	2,926
Income tax benefits from employee stock plans	2,017	342
Excess tax benefits from employee stock plans	(2,287)	(555)
Provision for excess and obsolete inventories	32	451
Deferred income taxes	(299)	(1,076)
Changes in operating assets and liabilities:		
Accounts receivable, net	(17,114)	(10,706)
Inventories	450	327
Prepaid expenses	2,505	(657)
Other current assets	(27)	1,061
Non-current net investment in sales-type leases	(239)	443
Other assets	176	(463)
Accounts payable	3,683	124
Accrued compensation	(7,586)	(4,665)
Accrued liabilities	(252)	537
Deferred service revenue	712	(42)
Deferred gross profit	5,149	6,166
Other long-term liabilities	254	133
Net cash provided by operating activities	1,117	4,132
Cash flows from investing activities:		
Acquisition of intangible assets and intellectual property	(139)	(48)
Software development for external use	(2,902)	(1,899)
Purchases of property and equipment	(2,551)	(3,300)
Net cash used in investing activities	(5,592)	(5,247)
Cash flows from financing activities:		
Proceeds from issuance of common stock under employee stock purchase and stock option plans	9,624	8,315
Employees' taxes paid related to restricted stock units	(349)	(211)
Common stock repurchases	(4,069)	—
Excess tax benefits from employee stock plans	2,287	555
Net cash provided by financing activities	7,493	8,659
Effect of exchange rate changes on cash and cash equivalents	9	(40)
Net increase in cash and cash equivalents	3,027	7,504

Cash and cash equivalents at beginning of period	104,531	62,313
Cash and cash equivalents at end of period	$107,558	$69,817

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

OMNICELL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Organization and Summary of Significant Accounting Policies

Description of the Company. Omnicell, Inc. ("Omnicell," "our," "us," "we," or the "Company") was incorporated in California in 1992 under the name Omnicell Technologies, Inc. and reincorporated in Delaware in 2001 as Omnicell, Inc. Our major products are automated medication supply control systems and medical adherence solutions which are sold in our principal market, which is the healthcare industry. Our market is primarily located in the United States and Canada.

Basis of presentation. These interim condensed consolidated financial statements are unaudited but reflect, in the opinion of management, all adjustments, consisting of normal recurring adjustments and accruals, necessary to present fairly the financial position of Omnicell and its subsidiaries as of March 31, 2014, the results of their operations, comprehensive income and cash flows for the three months ended March 31, 2014 and 2013. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (“GAAP”), have been condensed or omitted in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”). These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2013.

Our results of operations, comprehensive income and cash flows for the three months ended March 31, 2014 are not necessarily indicative of results that may be expected for the year ending December 31, 2014, or for any future period.

Use of estimates. GAAP requires management to make estimates and assumptions that affect the amounts reported in our consolidated financial statements and accompanying notes. Management bases its estimates on historical experience and various other assumptions believed to be reasonable. Although these estimates are based on management's best knowledge of current events and actions that may impact the company in the future, actual results may be different from the estimates. Our critical accounting policies are those that affect our financial statements materially and involve difficult, subjective or complex judgments by management. Those policies are revenue recognition, share-based compensation, inventory valuation, valuation of goodwill and purchased intangibles, valuation of long-lived assets and accounting for income taxes.

Principles of consolidation. The condensed consolidated financial statements include the accounts of our wholly-owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation.

Concentration of credit risk. Financial instruments that may potentially subject us to concentrations of credit risk consist principally of cash equivalents and accounts receivable. Cash equivalents are maintained with several financial institutions and may exceed the amount of insurance provided on such balances. The majority of our accounts receivable are derived from sales to customers for commercial applications. We perform ongoing credit evaluations of our customers’ financial condition and limit the amount of credit extended when deemed necessary but generally require no collateral. We maintain reserves for potential credit losses. Our products are broadly distributed and there was no single customer accounting for 10% or more of revenues in the three months ended March 31, 2014. Additionally, there was no single customer accounting for 10% or more of accounts receivable at March 31, 2014 or December 31, 2013. We believe that we have no significant concentrations of credit risk at March 31, 2014.

Dependence on suppliers. We have a supply agreement with one primary supplier for construction and supply of several sub-assemblies and inventory management of sub-assemblies used in our hardware products. There are no minimum purchase requirements. The contract may be terminated by either the supplier or by us without cause and at any time upon delivery of two months' notice. Purchases from this supplier for the three months ended March 31, 2014 and 2013 totaled approximately $8.9 million and $7.2 million, respectively.

There have been no material changes in our significant accounting policies as of and for the three months ended March 31, 2014, compared to the significant accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2013.

Table of Contents

Recently Adopted Accounting Standards

In July 2013, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. ASU 2013-11 requires an entity to present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows: to the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. We adopted the amendments in ASU 2013-11 in the first quarter of 2014. This update did not have a significant impact on our financial position, operating results or cash flows.

Table of Contents

Note 2. Net Income Per Share

Basic net income per share is computed by dividing net income for the period by the weighted average number of shares outstanding during the period, less shares subject to repurchase. Diluted net income per share is computed by dividing net income for the period by the weighted average number of shares, less shares subject to repurchase, plus, if dilutive, potential common stock outstanding during the period. Potential common stock includes the effect of outstanding dilutive stock options, restricted stock awards and restricted stock units computed using the treasury stock method. Since their impact is anti-dilutive, we excluded 347,265 and 1,865,589 shares from the calculations of diluted net income per share for the three months ended March 31, 2014 and 2013, respectively.

The calculation of basic and diluted net income per share is as follows (in thousands, except per share amounts):

	Three Months Ended March 31,	
	2014	2013
Basic:		
Net income	$6,194	$3,385
Weighted average shares outstanding — basic	35,225	33,900
Net income per share — basic	$0.18	$0.10
Diluted:		
Net income	$6,194	$3,385
Weighted average shares outstanding — basic	35,225	33,900
Add: Dilutive effect of employee stock plans	1,080	920
Weighted average shares outstanding — diluted	36,305	34,820
Net income per share — diluted	$0.17	$0.10

Table of Contents

Note 3. Cash and Cash Equivalents and Fair Value of Financial Instruments

Cash and cash equivalents consist of the following significant asset investment classes as of March 31, 2014 and December 31, 2013 (in thousands):

	March 31, 2014					
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash / Cash Equivalents	Security Classification
Cash	$52,906	$—	$—	$52,906	$52,906	N/A
Money market fund	54,652	—	—	54,652	54,652	Available for sale
Total cash and cash equivalents	$107,558	$—	$—	$107,558	$107,558	

c	December 31, 2013					
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash / Cash Equivalents	Security Classification
Cash	$38,823	$—	$—	$38,823	$38,823	N/A
Money market fund	65,708	—	—	65,708	65,708	Available for sale
Total cash and cash equivalents	$104,531	$—	$—	$104,531	$104,531	

The money market fund is a daily-traded cash equivalent with a price of $1.00, making it a Level 1 asset class, and its carrying cost closely approximates fair value. As demand deposit (cash) balances vary with the timing of collections and payments, the money market fund can cover any surplus or deficit, and thus is considered Available-for-sale. We did not hold any Level 2 and Level 3 assets or liabilities as of March 31, 2014 and December 31, 2013.

The following table shows our financial assets measured at fair value, on a recurring basis, with money market funds recorded within cash and cash equivalents (in thousands):

	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Total Fair Value
Money market fund at March 31, 2014	$54,652	$54,652
Money market fund at December 31, 2013	$65,708	$65,708

Note 4. Inventories

Inventories consist of the following (in thousands):

	March 31, 2014	December 31, 2013
Raw materials	$10,278	$10,765
Work in process	944	534
Finished goods	19,753	20,158
Total	$30,975	$31,457

Table of Contents

Note 5. Property and Equipment

Property and equipment consist of the following (in thousands):

	March 31, 2014	December 31, 2013
Equipment	$40,682	$40,180
Furniture and fixtures	5,296	5,260
Leasehold improvements	7,451	7,394
Purchased software	21,299	20,199
Construction in process	3,355	2,649
	78,083	75,682
Accumulated depreciation and amortization	(42,905)	(40,428)
Property and equipment, net	$35,178	$35,254

Depreciation and amortization of property and equipment totaled approximately $2.5 million and $2.7 million for the three months ended March 31, 2014 and 2013, respectively.

Table of Contents

Note 6. Net Investment in Sales-Type Leases

Our sales-type leases are for terms generally up to five years. Sales-type lease receivables are collateralized by the underlying equipment. The components of our net investment in sales-type leases are as follows (in thousands):

	March 31, 2014	December 31, 2013
Net minimum lease payments to be received	$18,351	$18,172
Less unearned interest income portion	1,397	1,455
Net investment in sales-type leases	16,954	16,717
Less current portion(1)	5,310	5,232
Non-current net investment in sales-type leases(2)	$11,644	$11,485

(1) A component of other current assets. This amount is net of an immaterial allowance for doubtful accounts as of March 31, 2014 and December 31, 2013.
(2) This amount is net of an immaterial allowance for doubtful accounts as of March 31, 2014 and December 31, 2013.

The minimum lease payments under sales-type leases as of March 31, 2014 were as follows (in thousands):

Remainder of 2014	$4,549
2015	5,230
2016	3,991
2017	3,042
2018	1,466
Thereafter	73
Total	$18,351

The following table summarizes the credit losses and recorded investment in sales-type leases, excluding unearned interest (in thousands):

	Allowance for Credit Losses	Recorded Investment in Sales-type Leases Gross	Recorded Investment in Sales-type Leases Net
Credit loss disclosure for March 31, 2014:			
Accounts individually evaluated for impairment	$ —	$—	$—
Accounts collectively evaluated for impairment	169	17,123	16,954
Ending balances: March 31, 2014	$ 169	$17,123	$16,954
Credit loss disclosure for December 31, 2013:			
Accounts individually evaluated for impairment	$ —	$—	$—
Accounts collectively evaluated for impairment	167	16,884	16,717
Ending balances: December 31, 2013	$ 167	$16,884	$16,717

The following table summarizes the activity for the allowance for credit losses for the investment in sales-type leases for the three months ended March 31, 2014 and 2013 (in thousands):

	Three Months Ended March 31,

	2014	2013
Allowance for credit losses, beginning of period	$167	$607
Current period provision	2	13
Direct write-downs charged against the allowance	—	(413)
Recoveries of amounts previously charged off	—	(17)
Allowance for credit losses, end of period	$169	$190

Table of Contents

Note 7. Goodwill and Intangible Assets

Goodwill

Goodwill is tested for impairment on an annual basis and between annual tests if events or circumstances indicate that an impairment loss may have occurred, and we write down these assets when impaired. We perform our annual impairment tests during the fourth quarter of each fiscal year using the closing balance sheet as of the last day of the third quarter.

During the three months ended March 31, 2014, we noted no indications of impairment or triggering events to cause us to review goodwill for potential impairment. We will conduct our annual goodwill testing during the fourth fiscal quarter.

There were no changes in the carrying amount of goodwill for the period from December 31, 2013 to March 31, 2014. Goodwill by reporting unit, which is the same for our operating segments are as follows (in thousands):

	Goodwill at December 31, 2013	Adjustments to Goodwill	Goodwill at March 31, 2014
Reporting units:			
Automation and Analytics	$28,543	$—	$28,543
Medication Adherence	82,800	—	82,800
Total	$111,343	$—	$111,343

Intangible Assets, net

There were no indefinite-lived intangible assets as of March 31, 2014 or December 31, 2013. Finite-lived intangible assets consist of the following (in thousands):

	March 31, 2014			December 31, 2013			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Amortization Life
Finite-lived intangibles:							
Customer relationships	$54,730	$5,775	$48,955	$54,730	$5,236	$49,494	5-30 years
Acquired technology	27,580	2,965	24,615	27,580	2,598	24,982	3-20 years
Patents	1,561	303	1,258	1,493	254	1,239	20 years
Trade name	6,890	1,145	5,745	6,890	1,003	5,887	3-12 years
Non-compete agreements	—	—	—	60	60	—	3 years
Total finite-lived intangibles	$90,761	$10,188	$80,573	$90,753	$9,151	$81,602	

Amortization expense totaled $1.1 million for both the three months ended March 31, 2014 and 2013. The amortization of acquired technology is included within product cost of sales and amortization of other acquired intangibles is included within selling, general and administrative expenses.

Table of Contents

Estimated future amortization expense of finite-lived intangible assets are as follows (in thousands):

Remainder of 2014	$3,191
2015	4,225
2016	3,857
2017	3,822
2018	3,714
Thereafter	61,764
Total	$80,573

Table of Contents

Note 8. Accrued Liabilities

Accrued liabilities consist of the following (in thousands):

	March 31, 2014	December 31, 2013
Rebates and lease buyouts	$2,036	$1,699
Advance payments from customers	3,778	4,971
Accrued Group Purchasing Organization (GPO) fees	2,558	2,324
Technology license purchase obligation, current portion	1,000	1,500
Taxes payable	2,406	1,664
Other	1,716	1,588
Total	$13,494	$13,746

Table of Contents

Note 9. Deferred Gross Profit

Deferred gross profit consists of the following (in thousands):

	March 31, 2014	December 31, 2013
Sales of medication and supply dispensing systems and packaging equipment, delivered and invoiced but not yet installed	$36,151	$29,040
Cost of revenues, excluding installation costs	(11,045)	(9,083)
Deferred gross profit	$25,106	$19,957

Note 10. Commitments

We lease properties in California, Florida, Illinois, Tennessee, and the United Kingdom. We also have smaller rented offices in Strongsville, Ohio, the United Arab Emirates, the People's Republic of China and the Federal Republic of Germany.

At March 31, 2014, the minimum payments under our operating leases for each of the five succeeding fiscal years were as follows (in thousands):

Remainder of 2014	$3,538
2015	5,408
2016	5,442
2017	5,178
2018	4,299
Thereafter	16,743
Total	$40,608

We purchase components from a variety of suppliers and use contract manufacturers to provide manufacturing services for our products. During the normal course of business, we issue purchase orders with estimates of our requirements several months ahead of the delivery dates. Our near-term commitments to our contract manufacturers and suppliers totaled $9.7 million as of March 31, 2014.

Table of Contents

Note 11. Contingencies

Legal Proceedings

On March 8, 2013, Bobbi Polanco (“Polanco”) filed a putative class action complaint in the United States District Court for the District of New Jersey (the "Court") against Omnicell and certain of our customers (Case No. 1:13-cv-01417-NLH-KLM) alleging breach of state security notification laws, violations of state consumer fraud laws, fraud, negligence and conspiracy relating to the theft of an Omnicell electronic device containing medication dispensing cabinet log files, including certain patient health information, and subsequent notification of this unauthorized disclosure of personal health information. Polanco is seeking an injunction against the defendants to prevent each of them from committing the acts complained of in the future and monetary damages, costs and expenses. On May 2, 2013, the Court entered an order to show cause which provided, in relevant part, that Polanco is required to show cause as to why the case should not be dismissed for lack of subject matter jurisdiction. On May 13, 2013, Polanco filed an amended complaint. On May 31, 2013, Omnicell filed a motion to dismiss the complaint on the grounds that Polanco failed to satisfy constitutional standing requirements and that she failed to state a claim against Omnicell for violating state data breach notification statutes, consumer fraud, common law fraud, negligence and conspiracy. Omnicell also joined in the arguments of the other defendants seeking dismissal. On July 1, 2013, Polanco filed an opposition to the motions to dismiss. On July 15, 2013, Omnicell filed its reply to the opposition from Polanco. In December 2013, the Court granted the defendants' motions to dismiss without prejudice. Polanco failed to file an appeal of the Court's decision by the January 27, 2014 deadline.

As required under ASC 450, Contingencies, we accrue for contingencies when we believe that a loss is probable and that we can reasonably estimate the amount of any such loss. We did not record any accrual for contingent liabilities associated with the legal proceedings described above based on our belief that any potential loss, while reasonably possible, was not probable. We believe that we have valid defenses with respect to legal proceedings pending against us. However, litigation is inherently unpredictable, and it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of this contingency or because of the diversion of management's attention and the creation of significant expenses.

Guarantees

As permitted under Delaware law and our certificate of incorporation and bylaws, we have agreed to indemnify our directors and officers against certain losses that they may suffer by reason of the fact that such persons are, were or become our directors or officers. The term of the indemnification period is for the director’s or officer’s lifetime and there is no limit on the potential amount of future payments that we could be required to make under these indemnification agreements. We have purchased a directors’ and officers’ liability insurance policy that may enable us to recover a portion of any future payments that we may be required to make under these indemnification agreements. Assuming the applicability of coverage and the willingness of the insurer to assume coverage and subject to certain retention, loss limits and other policy provisions, we believe it is unlikely that we will be required to pay any material amounts pursuant to these indemnification obligations. However, no assurances can be given that the insurers will not attempt to dispute the validity, applicability or amount of coverage without expensive and time-consuming litigation against the insurers.

Additionally, we undertake indemnification obligations in our ordinary course of business in connection with, among other things, the licensing of our products and the provision of our support services. In the ordinary course of our business, we have in the past and may in the future agree to indemnify another party, generally our business affiliates or customers, against certain losses suffered or incurred by the indemnified party in connection with various types of claims, which may include, without limitation, claims of intellectual property infringement, certain tax liabilities, our gross negligence or intentional acts in the performance of support services and violations of laws. The term of these indemnification obligations is generally perpetual. In general, we attempt to limit the maximum potential amount of future payments that we may be required to make under these indemnification obligations to the amounts paid to us by a customer, but in some cases the obligation may not be so limited. In addition, we have in the past and may in the future warrant to our customers that our products will conform to functional specifications for a limited period of time

following the date of installation (generally not exceeding 30 days) or that our software media is free from material defects. Sales contracts for certain of our medication packaging systems often include limited warranties for up to six months, but the periodic activity and ending warranty balances we record have historically been immaterial.

Table of Contents

From time to time, we may also warrant that our professional services will be performed in a good and workmanlike manner or in a professional manner consistent with industry standards. We generally seek to disclaim most warranties, including any implied or statutory warranties such as warranties of merchantability, fitness for a particular purpose, title, quality and non-infringement, as well as any liability with respect to incidental, consequential, special, exemplary, punitive or similar damages. In some states, such disclaimers may not be enforceable. If necessary, we would provide for the estimated cost of product and service warranties based on specific warranty claims and claim history. We have not been subject to any significant claims for such losses and have not incurred any material costs in defending or settling claims related to these indemnification obligations. Accordingly, we believe it is unlikely that we will be required to pay any material amounts pursuant to these indemnification obligations or potential warranty claims and, therefore, no material liabilities have been recorded for such indemnification obligations as of March 31, 2014 or December 31, 2013.

Note 12. Stockholders' Equity

Treasury Stock

2012 Stock Repurchase Program

On August 1, 2012, our Board of Directors established a stock repurchase program (the "2012 Repurchase Program") authorizing share repurchases of up to $50.0 million of our common stock, with no termination date. The timing, price and volume of repurchases will be based on market conditions, relevant securities laws and other factors. The stock repurchases may be made from time to time on the open market, in privately negotiated transactions or pursuant to a Rule 10b-18 plan. The 2012 Repurchase Program does not obligate us to repurchase any specific number of shares, and we may terminate or suspend the repurchase program at any time.

For the three months ended March 31, 2014, we repurchased a total of $4.1 million, or 145,737 shares, at an average cost of $27.92, including commissions. We did not repurchase any shares for the three months ended March 31, 2013.

From the inception of the 2012 Repurchase Program, we have repurchased a total of $25.0 million, or 1,030,382 shares at an average cost of $24.29 per share, including commissions. As of March 31, 2014, the maximum dollar value of shares that may yet be purchased under the plan is $25.0 million.

Note 13. Stock Option Plans and Share-Based Compensation

Description of Share-Based Plans

Equity Incentive Plan

For a detailed explanation of our stock plan and subsequent changes please refer back to our Note 16, Stock Option Plans, Share-Based Compensation and 401(k) Plan on our Annual Report on Form 10-K for the year ended December 31, 2013. At March 31, 2014, 2,457,760 shares of common stock were reserved for future issuance our 2009 Equity Incentive Plan, as amended (the "2009 Plan"), and $6.3 million of total unrecognized compensation cost related to non-vested stock options was expected to be recognized over a weighted average period of 2.8 years.

A summary of option activity under the 2009 Plan for the three months ended March 31, 2014 is presented below:

Options:	Number of Shares	Weighted-Average Exercise Price
	(in thousands)	
Outstanding at December 31, 2013	3,143	$ 15.82
Granted	241	$ 25.43
Exercised	(401)	$ 15.24
Forfeited	(38)	$ 16.54
Expired	(3)	$ 22.99
Outstanding at March 31, 2014	2,942	$ 16.67

Vested and expected to vest at March 31, 2014	2,909	$ 16.61
Exercisable at March 31, 2014	1,810	$ 15.08

Table of Contents

The aggregate intrinsic value of our options is calculated as the difference between the exercise price of the underlying options and the quoted price of our common stock at the end of the reporting period. The aggregate intrinsic value of options exercised under our stock plans for the three months ended March 31, 2014 and March 31, 2013 was $11.4 million and $8.3 million, respectively, determined as of the date of option exercise.

Restricted Stock and Restricted Stock Units

A summary of activity of both restricted stock and RSUs for the three months ended March 31, 2014 is presented below:

	Restricted Stock		Restricted Stock Units	
	Number of Shares	Weighted-Average Grant Date Fair Value Per Share	Number of Shares	Weighted-Average Grant Date Fair Value Per Share
	(in thousands)		(in thousands)	
Non-vested, December 31, 2013	52	$18.43	362	$17.15
Granted	—	$—	97	$25.54
Vested	—	$—	(31)	$15.69
Forfeited	—	$—	(14)	$15.45
Non-vested, March 31, 2014	52	$18.43	414	$19.27

The fair value of restricted stock is the product of the number of shares granted and the closing market price of our common stock on the grant date. Our unrecognized compensation cost related to non-vested restricted stock is approximately $7.2 million and is expected to be recognized over a weighted-average period of 2.8 years.

Performance-Based Restricted Stock Units

Performance-based restricted stock units ("PSUs") are an element of our executive compensation plans. In 2012, we granted 125,000 PSUs to our executive officer of which 62,500 became eligible for vesting upon the achievement of a certain level of shareholder return for 2012 as described below. In 2013, we granted 137,500 PSUs to our executive officers, all of which became eligible for vesting upon the achievement of a certain level of shareholder return for the period from January 1, 2013 through February 28, 2014, as described below. In 2014, we granted 132,500 PSUs to our executive officers, all, none or a portion of which may become eligible for vesting depending on the level of shareholder return for 2014. For a more detailed explanation of our PSUs and subsequent changes, please refer back to our Note 16, Stock Option Plans, Share-Based Compensation and 401(k) Plan on our Annual Report on Form 10-K for the year ended December 31, 2013.

Our unrecognized compensation cost related to non-vested performance-based restricted stock units at March 31, 2014 was approximately $2.8 million and is expected to be recognized over a weighted-average period of 1.5 years. For the three months ended March 31, 2014 and 2013, we recognized $0.5 million and $0.4 million, respectively, of compensation expense for the PSUs.

The following table shows the percent of PSUs granted in 2012 eligible for further time-based vesting based on our percentile placement:

Percentile Placement of Our Total Shareholder Return	% of PSUs Eligible for Time-Based Vesting
Below the 35th percentile	—%
At least the 35th percentile, but below the 50th percentile	50%
At least the 50th percentile	100%

On January 22, 2013, the Compensation Committee of our Board of Directors ("the Compensation Committee") confirmed 35.3% as the percentile rank of Omnicell's 2012 total stockholder return. This resulted in 50% of the 2012 PSU awards, or 62,500 shares, as eligible for further time-based vesting. The eligible performance-based restricted stock unit awards will vest as follows: 25% of the eligible shares vested immediately on January 22, 2013 with the

remaining eligible awards vesting in equal increments, semi-annually, over the subsequent three year period beginning on June 15th and December 15th of the year after the date of grant and each subsequent year. Vesting is contingent upon continued service.

Table of Contents

The following table shows the percent of PSUs granted in 2013 eligible for further time-based vesting based on our percentile placement:

Percentile Placement of Our Total Shareholder Return	% of PSUs Eligible for Time-Based Vesting
Below the 35th percentile	—%
At least the 35th percentile, but below the 50th percentile	50%
At least the 50th percentile	100%

On March 20, 2014, the Compensation Committee confirmed 63.94% as the percentile rank of Omnicell's 2013-2014 total stockholder return. This resulted in 100% of the 2013 PSU awards, or 137,500 shares, as eligible for further time-based vesting. The eligible performance-based restricted stock unit awards will vest as follows: 25% of the eligible shares vested immediately on March 20, 2014 with the remaining eligible awards vesting in equal increments, semi-annually, over the subsequent three year period beginning on June 15th and December 15th of the year after the date of grant and each subsequent year. Vesting is contingent upon continued service.

On February 5, 2014, the Compensation Committee approved PSU awards of 132,500 shares. If the minimum performance threshold is met as determined by the Compensation Committee in 2015, the eligible performance-based restricted stock unit awards will vest as follows: 25% of the eligible shares will vest immediately, with the remaining eligible awards vesting in equal increments, semi-annually, over the subsequent three year period beginning on June 15th and December 15th of the year after the date of grant and each subsequent year. Vesting is contingent upon continued service.

A summary of activity of the PSUs for the three months ended March 31, 2014 is presented below:

Performance-based Stock Units	Number of Shares	Weighted-Average Grant Date Fair Value Per Share
	(in thousands)	
Non-vested, December 31, 2013	225	$13.32
Granted	132	$16.59
Vested	(34)	$14.81
Forfeited	—	$—
Non-vested, March 31, 2014	323	$14.41

1997 Employee Stock Purchase Plan

We have an Employee Stock Purchase Plan (the “ESPP”) under which employees can purchase shares of our common stock based on a percentage of their compensation, but not greater than 15% of their earnings, up to a maximum of $25,000 of fair value per year. The purchase price per share must be equal to the lower of 85% of the fair value of the common stock at the beginning of a 24-month offering period or the end of each six-month purchasing period.

At the 2009 Annual Meeting of Stockholders, the stockholders approved an amendment to the ESPP, which added 2,622,426 shares to the reserve for future issuance. As of March 31, 2014, there were 846,891 shares reserved for future issuance under the ESPP. For the three months ended March 31, 2014, 254,009 shares of common stock were purchased under the ESPP. As of March 31, 2014, 4,484,664 shares had been issued under the ESPP.

As of March 31, 2014, our unrecognized compensation cost related to the shares to be purchased under our ESPP was approximately $1.4 million and is expected to be recognized over a weighted average period of 2.0 years.

Share-based Compensation

We account for share-based awards granted to employees and directors, including employee stock option awards, restricted stock, PSUs and RSUs issued pursuant to the 2009 Plan and employee stock purchases made under our ESPP using the estimated grant date fair value method of accounting in accordance with ASC 718, Stock Compensation.

Table of Contents

We value options and ESPP shares using the Black-Scholes-Merton option-pricing model. Restricted stock and time-based RSUs are valued at the grant date fair value of the underlying common shares. The PSUs are valued via Monte Carlo simulation.

The impact on our results for share-based compensation was as follows (in thousands):

	Three Months Ended March 31,	
	2014	2013
Cost of product and service revenues	$268	$305
Research and development expenses	369	289
Selling, general and administrative expenses	2,092	2,332
Total share-based compensation expenses	$2,729	$2,926

Note 14. Segments

Beginning with the acquisition of MTS, which was completed in May 2012, we have organized our business into two operating business segments. Previously, we reported segments based on the customers that our products were sold to, with the Acute Care segment primarily including products and services sold to hospital customers, and the Non-Acute Care segment primarily including products and services sold to customers outside of hospital settings. We are at a point where many of our Acute Care and Non-Acute Care customers are converging to provide services across the continuum of care. These customers seek automation and analytics products that function across the various facilities they manage and we find ourselves providing solutions across multiple types of care environments. These customers are also interested in obtaining higher levels of adherence to prescribed medication regimens that our blister card products provide. Our business has evolved to be managed more on a product basis and it has become more difficult to determine whether a customer is a hospital or a blend of hospitals and non-acute care facilities. Accordingly, beginning in 2014, we have realigned our segments to reflect the products we sell, regardless of who they are sold to.
The Automation and Analytics segment is organized around the design, manufacturing, selling and servicing of medication and supply dispensing systems, pharmacy inventory management systems, and related software.
The Medication Adherence segment includes primarily the manufacturing and selling of consumable medication blister cards, packaging equipment and ancillary products and services.
Prior period amounts in the table below have been recast to conform to the way we internally manage and monitor performance at the segment level during the current period.
We report segment information based on the management approach. The management approach designates the internal reporting used by the Chief Operating Decision Maker (the "CODM") for making decisions and assessing performance as the source of our operating segments. The CODM is our Chief Executive Officer. The CODM allocates resources to and assesses the performance of each operating segment, using information about its revenues, gross profit and income (loss) from operations. The CODM does not evaluate operating business segments using discrete asset information; accordingly, we do not report segment assets.
Since 1992, Omnicell has provided automation and business information solutions to healthcare facilities in general, but with a focus on acute care hospitals. We have developed product solutions that help optimize various workflows utilized in hospitals. We have also developed sophisticated sales, installation, and service capabilities to serve the specific and special needs of hospitals. As the healthcare market evolves, acute care facilities are beginning to merge operationally with non-acute care facilities. The new healthcare organizations desire medication and supply inventory control and business analytics across the continuum of care environments they serve. Our Automation and Analytics segment represents the products we sell to fulfill these needs.
Since 1984, MTS has provided medication adherence solutions to the non-acute care market. These solutions provide automated and semi-automated equipment to assist institutional and retail pharmacists in filling medication orders into blister cards, the primary method of medication control in non-acute care settings. Completing the product solution are the consumables used by institutional and retail pharmacists to make the medication adherence package. MTS has

developed process manufacturing capabilities as well as sales capabilities to market medication adherence solutions to institutional and retail pharmacies.

Table of Contents

As healthcare evolves, these medication adherence solutions are finding application in acute care settings as well. Our Medication Adherence segment represents all the products we sell to fulfill medication adherence needs through blister cards, blister card packaging equipment, and related software.

	Three Months Ended March 31, 2014			Three Months Ended March 31, 2013		
	Automation and Analytics	Medication Adherence	Total	Automation and Analytics	Medication Adherence	Total
Total revenues	$81,499	$20,265	$101,764	$68,713	$18,397	$87,110
Cost of revenues	34,940	12,329	47,269	30,276	11,467	41,743
Gross profit	$46,559	$7,936	$54,495	$38,437	$6,930	$45,367
Gross margin %	57.1 %	39.2 %	53.6 %	55.9 %	37.7 %	52.1 %
Operating expenses	37,402	7,139	44,541	33,104	8,094	41,198
Income (loss) from operations	$9,157	$797	$9,954	$5,333	$(1,164)	$4,169
Operating margin %	11.2 %	3.9 %	9.8 %	7.8 %	(6.3)%	4.8 %
Interest and other income (expense), net			(256)			(223)
Income before provision for income taxes			9,698			3,946
Provision for income taxes			3,504			561
Net income			$6,194			$3,385

For the three months ended March 31, 2014 and 2013, segment depreciation/amortization, and capital expenditures were as follows (amounts in thousands):

	Three Months Ended March 31, 2014			Three Months Ended March 31, 2013		
	Automation and Analytics	Medication Adherence	Total	Automation and Analytics	Medication Adherence	Total
Depreciation/Amortization	$2,898	$1,714	$4,612	$2,899	$1,573	$4,472
Capital Expenditures	$1,748	$803	$2,551	$1,000	$2,338	$3,338

Table of Contents

Note 15. Impairment of Software Development Costs

As part of the continuing integration of MTS, in the first quarter of 2013, we reorganized our management team, including the software development department, within the Medication Adherence segment. Through the end of the first quarter of 2013, the Medication Adherence segment had capitalized approximately $1.8 million of software development costs associated with a software solution under development which was intended to assist pharmacies in manual packaging of prescriptions. In connection with our financial statement close process for the quarter ended March 31, 2013, our management reassessed the viability of this project and the net realizable value of capitalized costs in light of its decision to change the related product road map and redesign this product based on evolving market demands. As part of this redesign process, new functionality and capabilities will need to be added to the product before commercialization. This redesign is intended to provide a more robust global platform providing larger scalability and significant functionality not contained in our current beta version. As such, we have determined we can no longer support the technological feasibility of this project in conjunction with our software capitalization policy. Therefore, we charged these costs, in the amount of