

OMNICELL, Inc
Form 10-Q
August 09, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

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 000-33043

Omnicell, Inc.

(Exact name of registrant as specified in its charter)

Delaware

94-3166458

(State or other jurisdiction

(I.R.S. Employer

of incorporation or organization)

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 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 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

Accelerated filer

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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

The number of shares of Registrant's common stock (par value \$0.001) outstanding as of August 1, 2013 was 34,840,670.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

OMNICELL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	June 30, 2013 (unaudited)	December 31, 2012 (1)
ASSETS		
Current assets:		
Cash and cash equivalents	\$87,334	\$62,313
Accounts receivable, net of allowances of \$560 and \$722 at June 30, 2013 and December 31, 2012, respectively	63,840	55,116
Inventories	26,360	26,903
Prepaid expenses	15,928	15,392
Deferred tax assets	11,860	11,860
Other current assets	7,899	9,172
Total current assets	213,221	180,756
Property and equipment, net	34,114	34,107
Non-current net investment in sales-type leases	13,222	13,228
Goodwill	111,343	111,407
Other intangible assets	83,468	85,550
Non-current deferred tax assets	985	993
Other assets	15,775	15,778
Total assets	\$472,128	\$441,819
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$17,459	\$18,255
Accrued compensation	11,239	11,613
Accrued liabilities	14,053	11,988
Deferred service revenue	20,434	20,449
Deferred gross profit	25,350	20,772
Total current liabilities	88,535	83,077
Non-current deferred service revenue	18,598	19,892
Non-current deferred tax liabilities	26,225	26,491
Other long-term liabilities	5,039	4,809
Total liabilities	138,397	134,269
Stockholders' equity:		
Total stockholders' equity	333,731	307,550
Total liabilities and stockholders' equity	\$472,128	\$441,819

(1) Information derived from our December 31, 2012 audited Consolidated Financial Statements.

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

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OMNICELL, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenues:				
Product revenues	\$75,581	\$59,269	\$144,817	\$107,793
Services and other revenues	18,105	16,115	35,979	31,734
Total revenues	93,686	75,384	180,796	139,527
Cost of revenues:				
Cost of product revenues	36,286	28,600	69,833	48,896
Cost of services and other revenues	8,032	7,408	16,228	15,506
Total cost of revenues	44,318	36,008	86,061	64,402
Gross profit	49,368	39,376	94,735	75,125
Operating expenses:				
Research and development	7,150	5,499	15,104	11,993
Selling, general and administrative	32,859	31,446	66,104	57,066
Total operating expenses	40,009	36,945	81,208	69,059
Income from operations	9,359	2,431	13,527	6,066
Interest and other income (expense), net	63	(73)	(159)	23
Income before provision for income taxes	9,422	2,358	13,368	6,089
Provision for income taxes	3,406	983	3,967	2,363
Net income	\$6,016	\$1,375	\$9,401	\$3,726
Net income per share-basic	\$0.17	\$0.04	\$0.28	\$0.11
Net income per share-diluted	\$0.17	\$0.04	\$0.27	\$0.11
Weighted average shares outstanding:				
Basic	34,450	33,390	34,177	33,377
Diluted	35,374	34,316	35,099	34,329

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

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OMNICELL, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,		
	2013	2012	2013	2012	
Net income	\$6,016	\$1,375	\$9,401	\$3,726	
Other comprehensive income (loss) and reclassification adjustments:					
Unrealized holding (losses) gains on securities arising during the period	—	(3) —	(1)
Changes in fair value of foreign currency forward hedges	—	65	(65) 65	
Foreign currency translation adjustment	5	(16) (198) (16)
Other comprehensive income (loss)	5	46	(263) 48	
Comprehensive income	\$6,021	\$1,421	\$9,138	\$3,774	

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

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OMNICELL, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Six Months Ended June 30,	
	2013	2012
Cash flows from operating activities:		
Net income	\$9,401	\$3,726
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,244	5,333
Loss on disposal of fixed assets	141	19
Impairment of software development costs	1,759	—
Provision for (recovery of) receivable allowance	63	335
Share-based compensation expense	5,613	4,420
Income tax benefits from employee stock plans	739	(156)
Excess tax benefits from employee stock plans	(1,258)	(901)
Provision for excess and obsolete inventories	742	254
Foreign currency remeasurement loss	—	(23)
Deferred income taxes	(258)	(535)
Changes in operating assets and liabilities:		
Accounts receivable, net	(8,757)	(287)
Inventories	(199)	4,409
Prepaid expenses	(536)	(1,114)
Other current assets	94	799
Net investment in sales-type leases	160	(780)
Other assets	(129)	(27)
Accounts payable	(796)	(817)
Accrued compensation	(374)	5,995
Accrued liabilities	2,065	(3,320)
Deferred service revenue	(1,294)	449
Deferred gross profit	4,578	268
Other long-term liabilities	230	711
Net cash provided by operating activities	21,228	18,758
Cash flows from investing activities:		
Purchases of short-term investments	—	—
Maturities of short-term investments	—	8,122
Acquisition of intangible assets and intellectual property	(64)	(249)
Software development for external use	(3,194)	(1,414)
Purchases of property and equipment	(5,711)	(4,087)
Business acquisition, net of cash acquired	—	(156,312)
Net cash used in investing activities	(8,969)	(153,940)
Cash flows from financing activities:		
Proceeds from issuance of common stock under employee stock purchase and stock option plans	11,549	3,627
Stock repurchases	—	(7,060)
Excess tax benefits from employee stock plans	1,258	901
Net cash provided by (used in) from financing activities	12,807	(2,532)
Effect of exchange rate changes on cash and cash equivalents	(45)	23

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Net increase (decrease) in cash and cash equivalents	25,021	(137,691)
Cash and cash equivalents at beginning of period	62,313	191,762
Cash and cash equivalents at end of period	\$87,334	\$54,071
Acquisition consideration accrued but not paid	\$—	\$(1,833)

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

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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 and supply control systems which are sold in our principal market, which is the healthcare industry. Our market is primarily located in the United States. On May 21, 2012, we completed our acquisition of MedPak Holdings, Inc. ("MedPak"). MedPak is the parent company of MTS Medication Technologies, Inc. ("MTS"), a worldwide provider of medication adherence packaging systems. This acquisition aligns us with the long-term trends of the healthcare market to manage the health of patients across the continuum of care. We can now serve both the acute care and non-acute care markets. Omnicell and MTS bring capabilities to each other that strengthen the product lines and expand the medication management coverage of both companies. Please refer to Note 14, "Business Acquisition" for more information regarding the transaction.

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 June 30, 2013, the results of their operations and comprehensive income for the three and six months ended June 30, 2013 and 2012 and their cash flows for the six months ended June 30, 2013 and 2012. 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, 2012.

Our results of operations, comprehensive income and cash flows for the six months ended June 30, 2013 are not necessarily indicative of results that may be expected for the year ending December 31, 2013, 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.

Foreign currency translation. We translate the assets and liabilities of our non-U.S. dollar functional currency subsidiaries into U.S. dollars using exchange rates in effect at the end of each period. Revenue and expenses for these

subsidiaries are translated using rates that approximate those in effect during the period. Gains and losses from these translations are recorded as foreign currency translation adjustments and included in accumulated other comprehensive income in stockholders' equity.

Fair value of financial instruments. We value our financial assets and liabilities on a recurring basis using the fair value hierarchy established in Accounting Standards Codification ("ASC") 820, Fair Value Measurements and Disclosures. ASC 820 describes three levels of inputs that may be used to measure fair value, as follows:

- Level 1 inputs, which include quoted prices in active markets for identical assets or liabilities;
- Level 2 inputs, which include observable inputs other than Level 1 inputs, such as quoted prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability;

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Level 3 inputs, which include unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the underlying asset or liability. Level 3 assets and liabilities include those whose fair value measurements are determined using pricing models, discounted cash flow methodologies or similar valuation techniques, as well as significant management judgment or estimation.

At June 30, 2013 and December 31, 2012, our financial assets, measured at fair value on a recurring basis, utilizing Level 1 inputs included money market funds, classified as cash equivalents. For these items, quoted market prices are readily available and fair value approximates carrying value. We do not currently have any material financial instruments, measured at fair value on a recurring basis, utilizing Level 2 or Level 3 inputs.

Classification of marketable securities. Securities held as investments for the indefinite future pending future spending requirements are classified as "Available-for-sale" and are carried at their fair value, with any unrealized gain or loss recorded to other comprehensive income until realized. At June 30, 2013 and December 31, 2012, we held \$53.0 million and \$38.9 million, respectively, of money market mutual funds classified as available-for-sale cash equivalents. We do not hold securities for purposes of trading.

Currency forward contracts. From time to time we enter into foreign currency forward contracts to protect our business from the risk that exchange rates may affect the eventual cash flows resulting from intercompany transactions between Omnicell and our foreign subsidiaries. These transactions primarily arise as a result of products manufactured in the U.S. and sold to foreign subsidiaries in U.S. dollars rather than the subsidiaries' functional currencies. These forward contracts are considered to be financial derivative instruments and are recorded at fair value in the balance sheet. Changes in fair value of these financial derivative instruments are either recognized in other comprehensive income (a component of stockholders' equity) or net income depending on whether the derivative has been designated and qualifies as a highly effective hedging instrument. At June 30, 2013 and December 31, 2012, we had no foreign currency forward contracts which qualify for hedge accounting.

Segment information. Prior to the acquisition of MTS, we managed our business on the basis of a single operating segment, and a single reporting unit within that segment per ASC 280, Segment Reporting. Beginning with the acquisition of MTS, which we completed in May 2012, we have organized our business into two operating business segments: Acute Care, which primarily includes products and services sold to hospital customers, and Non-Acute Care, which primarily includes products and services sold to customers outside of the hospital setting. The Acute Care segment is organized around the design, manufacturing, selling and servicing of medication and supply dispensing systems. The Non-Acute Care segment includes primarily the manufacturing and selling of consumable medication blister cards, packaging equipment and ancillary products and services, but also includes medication dispensing systems sold to non-acute care pharmacies and facilities. 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.

Revenue recognition. We earn revenues from sales of our medication control systems together with related consumables and services, and medical/surgical supply control systems with related services, which are sold in our principal market, which is the healthcare industry. Revenues related to consumable products are reported net of discounts provided to our customers. Our customer arrangements typically include one or more of the following deliverables:

- Products—Software-enabled equipment that manages and regulates the storage and dispensing of pharmaceuticals, consumable blister cards and packaging equipment and other medical supplies.
- Software—Additional software applications that enable incremental functionality of our equipment.
- Installation—Installation of equipment as integrated systems at customers' sites.

Post-installation technical support—Phone support, on-site service, parts and access to unspecified software upgrades and enhancements, if and when available.

Professional services—Other customer services such as training and consulting.

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We recognize revenue when the earnings process is complete, based upon our evaluation of whether the following four criteria have been met:

Persuasive evidence of an arrangement exists. We use signed customer contracts and signed customer purchase orders as evidence of an arrangement for equipment leases and sales. For service engagements, we use a signed services agreement and a statement of work to evidence an arrangement.

Delivery has occurred. Equipment and software product delivery is deemed to occur upon successful installation and receipt of a signed and dated customer confirmation of installation letter, providing evidence that we have delivered what a customer ordered. In instances of a customer self-installed installation, product delivery is deemed to have occurred upon receipt of a signed and dated customer confirmation letter. If a sale does not require installation, we recognize revenue on delivery of products to the customer, including transfer of title and risk of loss, assuming all other revenue criteria are met. We recognize revenue from sales of products to distributors upon delivery, when no contractual obligations for installation exists, assuming all other revenue criteria are met since we do not allow for rights of return or refund. For sales to distributors where we assume contractual installation obligations or new distributors whom we have not fully trained to install our products, the equipment and software product delivery is deemed to occur upon successful installation and receipt of a signed and dated customer confirmation of installation letter. For the sale of consumable blister cards, we recognize revenue when title and risk of loss of the products shipped have transferred to the customer, which usually occurs upon shipment from our facilities. Assuming all other revenue criteria are met, we recognize revenue for support services ratably over the related support services contract period, and we recognize revenue on training and professional services as those services are performed.

Fee is fixed or determinable. We assess whether a fee is fixed or determinable at the outset of the arrangement based on the payment terms associated with the transaction. We have established a history of collecting under the original contract without providing concessions on payments, products or services.

Collection is probable. We assess the probability of collecting from each customer at the outset of the arrangement based on a number of factors, including the customer's payment history and its current creditworthiness. If, in our judgment, collection of a fee is not probable, we defer the revenue until the uncertainty is removed, which generally means revenue is recognized upon our receipt of cash payment assuming all other revenue criteria are met. Our historical experience has been that collection from our customers is generally probable.

In arrangements with multiple deliverables, assuming all other revenue criteria are met, we recognize revenue for individual delivered items if they have value to the customer on a standalone basis. We allocate arrangement consideration at the inception of the arrangement to all deliverables using the relative selling price method. This method requires us to determine the selling price at which each deliverable could be sold if it were sold regularly on a standalone basis. When available, we use vendor-specific objective evidence ("VSOE") of fair value as the selling price. VSOE represents the price charged for a deliverable when it is sold separately or for a deliverable not yet being sold separately, the price established by management with the relevant authority. We consider VSOE to exist when approximately 80% or more of our standalone sales of an item are priced within a reasonably narrow pricing range (plus or minus 15% of the median rates). We have established VSOE of fair value for our post-installation technical support services and professional services. When VSOE of fair value is not available, third-party evidence ("TPE") of fair value for similar products and services is acceptable; however, our offerings and market strategy differ from those of our competitors, such that we cannot obtain sufficient comparable information about third parties' prices. If neither VSOE nor TPE are available, we use our best estimates of selling prices ("BESP"). We determine BESP considering factors such as market conditions, sales channels, internal costs and product margin objectives and pricing practices. We regularly review and update our VSOE, TPE and BESP information and obtain formal approval by appropriate levels of management.

The relative selling price method allocates total arrangement consideration proportionally to each deliverable on the basis of its estimated selling price. In addition, the amount recognized for any delivered items cannot exceed that which is not contingent upon delivery of any remaining items in the arrangement.

We also use the residual method of allocating the arrangement consideration in certain circumstances. We use the residual method to allocate total arrangement consideration between delivered and undelivered items for any arrangements entered into prior to January 1, 2011 and not subsequently materially-modified. The use of the residual

method is required by software revenue recognition rules that applied to sales of most of our products and services until the adoption of the new revenue recognition guidance. We also use the residual method to allocate revenue between the software products that enable incremental equipment functionality and thus are not deemed to deliver its essential functionality, and the related post-installation technical support, as these products and services continue to be accounted for under software revenue recognition

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rules. Under the residual method, the amount allocated to the undelivered elements equals VSOE of fair value of these elements. Any remaining amounts are attributed to the delivered items and are recognized when those items are delivered.

A portion of our sales are made through multi-year lease agreements. Under sales-type leases, we recognize revenue for our hardware and software products net of lease execution costs such as post-installation product maintenance and technical support, at the net present value of the lease payment stream once our installation obligations have been met. We optimize cash flows by selling a majority of our non-U.S. government leases to third-party leasing finance companies on a non-recourse basis. We have no obligation to the leasing company once the lease has been sold. Some of our sales-type leases, mostly those relating to U.S. government hospitals, are retained in-house. Interest income in these leases is recognized in product revenue using the effective interest method.

Accounts receivable and notes receivable (net investment in sales type leases). We actively manage our accounts receivable to minimize credit risk. We typically sell to customers for which there is a history of successful collection. New customers are subject to a credit review process, which evaluates that customer's financial position and ability to pay. We continually monitor and evaluate the collectability of our trade receivables based on a combination of factors. We record specific allowances for doubtful accounts when we become aware of a specific customer's impaired ability to meet its financial obligation to us, such as in the case of bankruptcy filings or deterioration of financial position. Uncollectible amounts are charged off against trade receivables and the allowance for doubtful accounts when we make a final determination that there is no reasonable expectation of recovery. Estimates are used in determining our allowances for all other customers based on factors such as current trends, the length of time the receivables are past due and historical collection experience. While we believe that our allowance for doubtful accounts receivable is adequate and that the judgment applied is appropriate, such estimated amounts could differ materially from what will actually be uncollectible in the future.

The retained in-house leases discussed above are considered financing receivables. Our credit policies and evaluation of credit risk and write-off policies are applied alike to trade receivables and the net-investment in sales-type leases. For both, an account is generally past due after thirty days. The financing receivables also have customer-specific reserves for accounts identified for specific impairment and a non-specific reserve applied to the remaining population, based on factors such as current trends, the length of time the receivables are past due and historical collection experience. The retained in-house leases are not stratified by portfolio or class. Financing receivables which are reserved are generally transferred to cash-basis accounting so that revenue is recognized only as cash is received. However, the cash basis accounts continue to accrue interest.

Sales of accounts receivable. We record the sale of our accounts receivables as "true sales" in accordance with accounting guidance for transfers and servicing of financial assets. During the three months ended June 30, 2013 and 2012, we transferred non-recourse accounts receivable totaling \$10.6 million and \$15.7 million, respectively, which approximated fair value, to third-party leasing companies. During the six months ended June 30, 2013 and 2012, we transferred non-recourse accounts receivable totaling \$20.9 million and \$27.8 million, respectively, which approximated fair value, to third-party leasing companies. At June 30, 2013 and December 31, 2012, accounts receivable included \$0.8 million and \$0.7 million, respectively, due from third-party leasing companies for transferred non-recourse accounts receivable.

Concentration in revenues and in accounts receivable. There was no single customer accounting for 10% or more of revenues in the three and six months ended June 30, 2013. Additionally, there was no single customer accounting for 10% or more of accounts receivable at June 30, 2013 or December 31, 2012. At June 30, 2013, we believe that we have no significant concentrations of credit risk.

Accounting policy for shipping costs. Outbound freight billed to customers is recorded as product revenue. The related shipping and handling cost is expensed as part of selling, general and administrative expense. Such shipping and handling expenses totaled \$1.6 million and \$0.8 million for the three months ended June 30, 2013 and 2012, respectively. Shipping and handling expenses totaled \$3.0 million and \$1.5 million for the six months ended June 30, 2013 and 2012, respectively.

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 June 30, 2013 and 2012 totaled approximately \$6.7 million and \$5.2 million, respectively. Purchases from this supplier for the six months ended June 30, 2013 and 2012 totaled approximately \$13.9 million and \$11.5 million, respectively.

Income taxes. We record an income tax provision for the anticipated tax consequences of the reported results of operations. In accordance with GAAP, the provision for income taxes is computed using the asset and liability method, under which deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for operating losses and tax credit carry forwards.

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Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply in the periods in which those tax assets and liabilities are expected to be realized. In the event that we determine all or part of the net deferred tax assets are not realizable in the future, we will record a valuation allowance that would be charged to earnings in the period such determination is made.

In accordance with ASC 740, Tax Provisions, we recognize the tax benefit from an uncertain tax position if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of GAAP and complex tax laws. Resolution of these uncertainties in a manner inconsistent with management's expectations could have a material impact on our financial condition and operating results.

We provide for income taxes for each interim period based on the estimated annual effective tax rate for the year, adjusting for discrete items in the quarter in which they arise. The annual effective tax rate before discrete items was 38.7% and 40.9% for the six months ended June 30, 2013 and 2012, respectively. The 2013 annual effective tax rate differed from the statutory rate of 35.0% primarily due to the unfavorable impact of state income taxes, non-deductible equity charges, and other non-deductible expenditures, which were partially offset by the federal research and development credit claimed and the domestic production activities deduction. The 2012 annual effective tax rate differed from the statutory rate of 35.0% primarily due to the unfavorable impact of state income taxes, non-deductible equity charges, and other non-deductible expenditures, which were partially offset by the domestic production activities deduction.

Recently Adopted Accounting Standards

In February 2013, the Financial Accounting Standards Board ("FASB") issued 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (AOCI), which aims to improve the reporting of reclassifications out of AOCI. This update requires an entity to report the effect of significant reclassifications out of AOCI on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. For public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2012. We adopted this guidance in the first quarter of 2013. This update did not have any significant impact on our financial position, operating results or cash flows.

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 1,581,335 and 2,103,021 shares from the calculations of diluted net income per share for the six months ended June 30, 2013 and 2012, respectively.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Basic:				
Net income	\$6,016	\$1,375	\$9,401	\$3,726
Weighted average shares outstanding — basic	34,450	33,390	34,177	33,377
Net income per share — basic	\$0.17	\$0.04	\$0.28	\$0.11
Diluted:				
Net income	\$6,016	\$1,375	\$9,401	\$3,726
Weighted average shares outstanding — basic	34,450	33,390	34,177	33,377
Add: Dilutive effect of employee stock plans	924	926	922	952
Weighted average shares outstanding — diluted	35,374	34,316	35,099	34,329
Net income per share — diluted	\$0.17	\$0.04	\$0.27	\$0.11

Note 3. Cash and Cash Equivalents, Short-term Investments and Fair Value of Financial Instruments

Cash and cash equivalents and short-term investments consist of the following significant investment asset classes, with disclosure of amortized cost, gross unrealized gains and losses and fair value as of June 30, 2013 and December 31, 2012 (in thousands):

	June 30, 2013						
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash / Cash Equivalents	Short-term Investments	Security Classification
Cash	\$34,364	\$—	\$—	\$34,364	\$34,364	\$—	N/A
Money market funds	52,970	—	—	52,970	52,970	—	Available for sale
Total cash, cash equivalents and short-term investments	\$87,334	\$—	\$—	\$87,334	\$87,334	\$—	
c							
	December 31, 2012						
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash / Cash Equivalents	Short-term Investments	Security Classification
Cash	\$23,422	\$—	\$—	\$23,422	\$23,422	\$—	N/A
Money market funds	38,892	—	1	38,891	38,891	—	Available for sale
Total cash, cash equivalents and short-term investments	\$62,314	\$—	\$1	\$62,313	\$62,313	\$—	

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.

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The following table displays the 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)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
At June 30, 2013				
Money market funds	\$52,970	\$—	\$—	\$52,970
Total	\$52,970	\$—	\$—	\$52,970
At December 31, 2012				
Money market funds	\$38,891	\$—	\$—	\$38,891
Total	\$38,891	\$—	\$—	\$38,891

Current assets and current liabilities are recorded at amortized cost, which approximates fair value due to the short-term maturities implied.

Note 4. Inventories

Inventories consist of the following (in thousands):

	June 30, 2013	December 31, 2012
Raw materials	\$9,842	\$9,994
Work in process	848	385
Finished goods	15,670	16,524
Total	\$26,360	\$26,903

Note 5. Property and Equipment

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

	June 30, 2013	December 31, 2012
Equipment	\$34,716	\$32,528
Furniture and fixtures	5,104	5,126
Leasehold improvements	7,139	6,992
Purchased software	19,735	19,870
Capital in process	2,812	2,693
	69,506	67,209
Accumulated depreciation and amortization	(35,392)	(33,102)
Property and equipment, net	\$34,114	\$34,107

Depreciation and amortization of property and equipment totaled approximately \$2.9 million and \$1.9 million for the three months ended June 30, 2013 and 2012, respectively. Depreciation and amortization of property and equipment totaled approximately \$5.6 million and \$3.5 million for the six months ended June 30, 2013 and 2012, respectively.

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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):

	June 30, 2013	December 31, 2012
Net minimum lease payments to be received	\$19,919	\$19,665
Less unearned interest income portion	1,164	1,205
Net investment in sales-type leases	18,755	18,460
Less current portion(1)	5,533	5,232
Non-current net investment in sales-type leases(2)	\$13,222	\$13,228

(1) A component of other current assets. This amount is net of allowance for doubtful accounts of \$0.1 million as of June 30, 2013 and \$0.5 million as of December 31, 2012.

(2) This amount is net of allowance for doubtful accounts of \$0.1 million as of June 30, 2013 and \$0.1 million as of December 31, 2012.

The minimum lease payments under sales-type leases as of June 30, 2013 were as follows (in thousands):

2013 (remaining six months)	\$3,165
2014	5,589
2015	4,499
2016	3,238
2017	2,493
Thereafter	935
Total	\$19,919

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 June 30, 2013:			
Accounts individually evaluated for impairment	\$ 47	\$47	\$—
Accounts collectively evaluated for impairment	137	18,892	18,755
Ending balances: June 30, 2013	\$ 184	\$18,939	\$18,755
Credit loss disclosure for December 31, 2012:			
Accounts individually evaluated for impairment	\$ 489	\$489	\$—
Accounts collectively evaluated for impairment	118	18,578	18,460
Ending balances: December 31, 2012	\$ 607	\$19,067	\$18,460

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The following table summarizes the activity for the allowance for credit losses for the investment in sales-type leases for the three and six months ended June 30, 2013 and 2012 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30	
	2013	2012	2013	2012
Allowance for credit losses, beginning of period	\$190	\$257	\$607	\$284
Current period provision (reversal)	6	422	19	422
Direct write-downs charged against the allowance	—	—	(413) —
Recoveries of amounts previously charged off	(12) (20) (29) (47
Allowance for credit losses, end of period	\$184	\$659	\$184	\$659

Note 7. Goodwill and Other Intangible Assets

Under ASC 350, Intangibles—Goodwill and Other, goodwill is not subject to amortization. We evaluate goodwill for impairment at least annually or more frequently if events and changes in circumstances suggest that the carrying amount may not be recoverable.

Activity in goodwill by reporting units, which are the same as our operating segments, for the six months ended June 30, 2013 consists of the following (in thousands):

	Goodwill at December 31, 2012	Adjustments to Goodwill	Goodwill at June 30, 2013
Reporting units:			
Acute Care	\$28,543	\$—	\$28,543
Non-Acute Care	82,864	(64) 82,800
Total	\$111,407	\$(64) \$111,343

Goodwill acquired reflects the May 21, 2012 acquisition of MedPak by Omnicell. MedPak is the parent company of MTS, a worldwide provider of medication adherence packaging systems. The acquired goodwill was assigned to the new reporting unit called Non-Acute Care, created as a result of the MTS acquisition. During the first quarter of 2013, we reduced goodwill by approximately \$0.1 million due to the adjustment to the fair value of an acquired foreign currency forward contract previously carried in a component of stockholder's equity.

There were no indefinite-life intangibles at either June 30, 2013 or