FRONTIER COMMUNICATIONS CORP
Form 424B3
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Ivan Seidenberg
Chairman and Chief Executive Officer

Verizon Communications Inc.

140 West Street
New York, New York 10007

May 28, 2010

To the Stockholders of Verizon Communications Inc.:

As previously announced, Verizon Communications Inc., which we refer to as Verizon, will spin off shares of New Communications Holdings Inc., a subsidiary of Verizon, which we refer to as Spinco, for the benefit of our stockholders.

Spinco will hold defined assets and liabilities of the local exchange business and related landline activities of Verizon in Arizona, Idaho, Illinois, Indiana, Michigan, Nevada, North Carolina, Ohio, Oregon, South Carolina, Washington, West Virginia and Wisconsin, and in portions of California bordering Arizona, Nevada and Oregon, collectively referred to as the Spinco territory, including Internet access and long distance services and broadband video provided to designated customers in the Spinco territory. In connection with the spin-off, Verizon and its subsidiaries will receive from Spinco $3.333 billion in aggregate value, comprised of $3.083 billion in the form of cash and $250 million in the form of a debt reduction. Immediately following the spin-off, Spinco will merge with and into Frontier Communications Corporation, which we refer to as Frontier. As a result, Verizon stockholders will receive Frontier common stock rather than shares of Spinco. After the merger, Frontier will continue to be a separately traded public company and will then own and operate the combined businesses of Spinco and Frontier.

As a result of the merger, Verizon stockholders will receive an aggregate number of shares of Frontier common stock equal to (1) $5,247,000,000, divided by (2) the Frontier average price, which is the average of the volume-weighted averages of the trading prices of Frontier common stock for the 30 consecutive trading days ending on the third trading day before the closing of the merger, provided that if an ex-dividend date occurs during this 30 day period, then the trading price for a share of Frontier common stock for each day before the stock begins trading ex-dividend will be reduced for purposes of this calculation by the amount of the dividend payable. The aggregate number of shares of Frontier common stock to be issued pursuant to the merger agreement will therefore change depending on the Frontier average price and will not be known until the closing of the merger. The merger agreement provides that if the Frontier average price, as calculated, exceeds $8.50, then the Frontier average price will be $8.50, and if the Frontier average price, as calculated, is less than $7.00, then the Frontier average price will be $7.00.

For example, if the closing of the merger had occurred on May 24, 2010, prior to the elimination of fractional shares, Verizon stockholders would have received an aggregate of 672,740,418 shares of Frontier common stock in the merger. This amount would have represented approximately 68.2% of the combined company s equity immediately after the closing of the merger if the closing had occurred on that date. Based on these assumptions, each Verizon stockholder would have received one share of Frontier common stock for approximately every 4.2 shares of Verizon common stock the Verizon stockholder owned on the assumed record date for the spin-off. For a more complete discussion of the calculation of the number of shares of Frontier common stock to be issued, see page 41 of this information statement/prospectus.

If the number of shares of Frontier common stock that the Verizon stockholder is entitled to receive results in or includes a fraction of a share of Frontier common stock, that stockholder will receive cash representing the value of the fractional share of Frontier common stock. While we expect that the receipt of Frontier common stock in the merger will be tax-free to Verizon stockholders, they will be required to pay tax on any cash payment that they receive.

Verizon stockholders will not be required to pay for any shares of Frontier common stock they will receive and will also retain all of their shares of Verizon common stock.

Verizon s Board of Directors has determined that the spin-off and the merger with Frontier are advisable and in the best interests of Verizon and its stockholders. Verizon has approved this transaction as the current sole stockholder of Spinco, and Verizon stockholders are not required, and are not being asked, to vote on the spin-off or the merger.

This information statement/prospectus contains important information describing Spinco, the combined company and the terms of the spin-off and the merger, including the calculation of the number of shares of Frontier common stock that Verizon stockholders will receive. It is also a prospectus relating to the Frontier common stock that Verizon stockholders will receive in the merger. Please read it carefully.

We look forward to completing this transaction.

Sincerely,

Neither the Securities and Exchange Commission nor any state securities regulator has approved or disapproved the merger described in this information statement/prospectus or the Frontier common stock to be issued pursuant to the merger agreement, or determined if this information statement/prospectus is accurate or adequate. Any representation to the contrary is a criminal offense.

The date of this information statement/prospectus is May 28, 2010.

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WHERE YOU CAN FIND ADDITIONAL INFORMATION

Verizon stockholders who have questions regarding the spin-off, the merger or any other matter described in this information statement/prospectus should contact:

Investor Relations

Verizon Communications Inc.

One Verizon Way

Basking Ridge, NJ 07920

Telephone: (212) 395-1525

Spinco has filed a registration statement on Form 10 (File No. 000-53950) with the Securities and Exchange Commission, referred to as the SEC, to register the class of common stock of Spinco that will be distributed to Verizon stockholders in the spin-off. This information statement/prospectus is included in the registration statement on Form 10.

In addition, Frontier has filed a registration statement on Form S-4 (File No. 333-160789) with the SEC, of which this information statement/prospectus is a part.

This information statement/prospectus incorporates additional information about Frontier that is not included in or delivered with this information statement/prospectus. Copies of Frontier s filings with the SEC are available to recipients of this information statement/prospectus without charge by request made to Frontier in writing, by telephone or by e-mail with the following contact information or through Frontier s website at www.frontier.com:

Frontier Communications Corporation

Attn: Investor Relations Department

3 High Ridge Park

Stamford, Connecticut 06905

Telephone: (866) 491-5249

E-mail: frontier@frontiercorp.com

Frontier makes available on its website at www.frontier.com its Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and all amendments to these reports as soon as reasonably practicable after it files these materials with, or furnishes these materials to, the SEC. Frontier s filings with the SEC are available to the public over the Internet at the SEC s website at www.sec.gov, or at the SEC s public reference room located at 100 F Street, N.E., Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference room.

ALL INFORMATION CONTAINED IN THIS INFORMATION STATEMENT/PROSPECTUS WITH RESPECT TO VERIZON OR SPINCO AND THEIR RESPECTIVE SUBSIDIARIES HAS BEEN PROVIDED BY VERIZON. ALL OTHER INFORMATION CONTAINED IN THIS INFORMATION STATEMENT/PROSPECTUS, INCLUDING PRO FORMA INFORMATION, HAS BEEN PROVIDED BY FRONTIER.

CERTAIN DEFINITIONS

Unless the context otherwise requires, references in this information statement/prospectus to Frontier mean Frontier Communications Corporation, together with its subsidiaries, references to Verizon mean Verizon Communications Inc., together with its subsidiaries, and references to the combined company mean Frontier Communications Corporation, together with its subsidiaries, following the completion of the transactions (as defined herein). Neither Cellco Partnership doing business as Verizon Wireless, referred to as Cellco, nor any of its subsidiaries is deemed to be a subsidiary or an affiliate of Verizon for purposes of the distribution agreement or the merger agreement (each as defined in this information statement/prospectus). This information statement/prospectus describes Spinco as if it had the assets, liabilities and customers that will be transferred to it prior to the completion of the spin-off and the merger for all periods and dates presented.

Pro forma condensed combined financial information in this information statement/prospectus, and the phrase on a pro forma basis, give pro forma effect to the transactions (as defined herein), including, among other things, the incurrence of indebtedness by Spinco to finance the special cash payment (as defined herein) and the expected repayment, on June 1, 2010, of $175 million of indebtedness of Verizon s Separate Telephone Operations, that would otherwise have constituted distribution date indebtedness (as defined herein), all as if they had occurred on January 1, 2009, for statement of operations purposes, and on March 31, 2010, for balance sheet purposes. See Summary Historical Consolidated and Combined Financial Information and Unaudited Pro Forma Condensed Combined Financial Information Pro Forma Combined and Unaudited Pro Forma Condensed Combined Financial Information.

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QUESTIONS AND ANSWERS

Q: **What are the transactions described in this information statement/prospectus?**

A: References to the transactions are to the spin-off, the merger and the related transactions to be entered into by Verizon, Spinco and Frontier, including their respective affiliates, as described under The Transactions and elsewhere in this information statement/prospectus.

Q: **What will happen in the spin-off?**

A: Pursuant to the distribution agreement, dated as of May 13, 2009, as amended by Amendment No. 1 thereto, dated as of July 24, 2009, and Amendment No. 2 thereto, dated as of March 23, 2010, by and between Verizon and Spinco, referred to as the distribution agreement, Verizon will contribute to Spinco defined assets and liabilities of the local exchange business and related landline activities of Verizon in Arizona, Idaho, Illinois, Indiana, Michigan, Nevada, North Carolina, Ohio, Oregon, South Carolina, Washington, West Virginia and Wisconsin, and in portions of California bordering Arizona, Nevada and Oregon, collectively referred to as the Spinco territory, including Internet access and long distance services and broadband video provided to designated customers in the Spinco territory, collectively referred to as the Spinco business. In addition, the combined company will also serve approximately 300 customers in a portion of Virginia bordering West Virginia.

In connection with these contributions, Verizon will receive from Spinco $3.333 billion in aggregate value in the form of:

- a special cash payment of $3,083 million (referred to as the special cash payment)

- a reduction in the consolidated indebtedness of Verizon of $250 million as a result of pre-existing long-term indebtedness to third parties of Verizon subsidiaries that conduct the Spinco business (referred to as the distribution date indebtedness) becoming the consolidated indebtedness of Spinco as a result of the spin-off (and, as a result of the merger, becoming part of the consolidated indebtedness of the combined company), referred to as the Verizon debt reduction.

Also in connection with these contributions, Spinco will issue additional shares of Spinco common stock to Verizon, which will be distributed in the spin-off as described below.

On April 12, 2010, Spinco issued $500,000,000 principal amount of 7.875% Senior Notes due 2015, $1,100,000,000 principal amount of 8.250% Senior Notes due 2017, $1,100,000,000 principal amount of 8.500% Senior Notes due 2020 and $500,000,000 principal amount of 8.750% Senior Notes due 2022 (referred to collectively as the notes). The notes were issued in a private transaction (referred to as the notes offering) that was not subject to the registration requirements of the Securities Act of 1933, as amended. The gross proceeds of the notes offering, plus an amount in cash contributed by Frontier that equals the amount of interest that will accrue on the notes from April 12, 2010 to October 1, 2010, were deposited into an escrow account. Immediately prior to the spin-off and the completion of the merger, the gross proceeds of the notes offering (less the initial purchasers discount) will be released from the escrow account and used to make the special cash payment by Spinco to Verizon, with any such amount in excess of the special cash payment to be retained by the combined company. Spinco completed the notes offering in order to provide debt financing to finance the special cash payment, referred to as the special cash payment financing, as required by the Agreement and Plan of Merger, dated as of May 13, 2009, as amended by Amendment No. 1 thereto, dated as of July 24, 2009, by and among Verizon, Spinco and Frontier, referred to as the merger agreement. See Financing of the Combined Company.

Immediately prior to the merger, Verizon will spin off Spinco by distributing all of the shares of Spinco common stock to Computershare Trust Company, N.A., as third-party distribution agent, to be held for the benefit of Verizon stockholders. Spinco will then merge with and into Frontier, and the shares of Spinco common stock will be immediately converted into that number of shares of Frontier common stock that

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Verizon stockholders will be entitled to receive in the merger. The third-party distribution agent will then distribute shares of Frontier common stock and cash in lieu of fractional shares to Verizon stockholders on a pro rata basis in accordance with the terms of the merger agreement.

Q: **What will happen in the merger?**

A: In the merger, Spinco will merge with and into Frontier in accordance with the terms of the merger agreement. Spinco will no longer be a separate company, and Frontier will survive the merger as a stand-alone company holding and conducting the combined business operations of Frontier and Spinco.

Q: **What will Verizon stockholders be entitled to receive pursuant to the merger?**

A: As a result of the merger, Verizon stockholders will receive an aggregate number of shares of Frontier common stock equal to (1) $5,247,000,000, divided by (2) the Frontier average price, which is the average of the volume-weighted averages of the trading prices of Frontier common stock for the 30 consecutive trading days ending on the third trading day before the closing of the merger, referred to as the Frontier average price calculation period, provided that if an ex-dividend date occurs during this 30 day period, then the trading price for a share of Frontier common stock for each day before the stock begins trading ex-dividend will be reduced for purposes of this calculation by the amount of the dividend payable. Frontier has declared a dividend of $0.25 per share of its common stock, payable on June 30, 2010, to holders of record of its common stock at the close of business on June 9, 2010, and therefore it is expected that the calculation of the Frontier average price will reflect adjustments to the trading price for shares of Frontier common stock before June 7, 2010, reducing the trading prices for purposes of this calculation for those days by $0.25. The aggregate number of shares of Frontier common stock to be issued pursuant to the merger agreement will therefore change depending on the Frontier average price. However, the merger agreement provides that if the Frontier average price, as calculated, exceeds $8.50, then the Frontier average price will be $8.50, and if the Frontier average price, as calculated, is less than $7.00, then the Frontier average price will be $7.00. These limitations on the Frontier average price are referred to as the collar.

Depending on the trading prices of Frontier common stock prior to the closing of the merger and before accounting for the elimination of fractional shares, Verizon stockholders will collectively own between approximately 66% and 71% of the combined company s outstanding equity immediately following the closing of the merger, and Frontier stockholders will collectively own between approximately 29% and 34% of the combined company s outstanding equity immediately following the closing of the merger. Each Verizon stockholder will receive a number of shares of Frontier common stock equal to the product of the aggregate number of shares of Frontier common stock to be issued pursuant to the merger agreement multiplied by a fraction, the numerator being the number of shares of Verizon common stock owned by that stockholder as of the record date for the spin-off and the denominator being the total number of shares of Verizon common stock outstanding as of that record date plus the total number of shares of Verizon common stock issuable pursuant to employee stock options held on that record date and exercised by the holders thereof between that record date and the date of the spin-off.

For example, if the closing of the merger had occurred on May 24, 2010, based on the average of the volume-weighted averages of the trading prices of Frontier common stock for the 30 consecutive trading days ending May 19, 2010 (the third trading day before May 24, 2010), as reported by the New York Stock Exchange, referred to as the NYSE, the Frontier average price would have equaled $7.80. Prior to the elimination of fractional shares, Verizon stockholders would have received an aggregate of 672,740,418 shares of Frontier common stock in the merger. This amount would have represented approximately 68.2% of the combined company s equity immediately after the closing of the merger if the closing had occurred on that date.

Based on these assumptions, each Verizon stockholder would have received one share of Frontier common stock for approximately every 4.2 shares of Verizon common stock the Verizon stockholder owned on the assumed record date for the spin-off. However, any change in the Frontier average price from the sample calculation of the Frontier average price used in the above example will, subject to the collar, cause the

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aggregate number of shares of Frontier common stock to be issued pursuant to the merger agreement (and the per share consideration to be received by Verizon stockholders in the merger) to change. In addition, any change in the number of shares of Verizon common stock outstanding prior to the record date of the spin-off (together with any shares of Verizon common stock issued pursuant to the exercise of Verizon stock options between the record date for the spin-off and the date of the spin-off) will cause the per share consideration to be received by Verizon stockholders to change.

No fractional shares of Frontier common stock will be issued to Verizon stockholders in the merger. Each Verizon stockholder will receive a cash payment in lieu of any fractional share of Frontier common stock to which he or she would otherwise be entitled. See The Transaction Agreements Merger Agreement Merger Consideration and Material United States Federal Income Tax Consequences of the Spin-Off and the Merger The Merger.

Q: **Will Verizon stockholders who sell their shares of Verizon common stock shortly before the completion of the spin-off and the merger still be entitled to receive shares of Frontier common stock with respect to the shares of Verizon common stock that were sold?**

A: It is currently expected that beginning not earlier than two business days before June 7, 2010, which is the record date for the spin-off, and continuing through the closing date of the merger (or the previous business day, if the merger closes before the opening of trading in Verizon common stock and Frontier common stock on the NYSE on the closing date), there will be two markets in Verizon common stock on the NYSE and on The NASDAQ Stock Market: a regular way market and an ex-distribution market.

If a Verizon stockholder sells shares of Verizon common stock in the regular way market under the symbol VZ during this time period, that Verizon stockholder will be selling both his or her shares of Verizon common stock and the right (represented by a due-bill) to receive shares of Spinco common stock that will be converted into shares of Frontier common stock, and cash in lieu of fractional shares (if any), at the closing of the merger. Verizon stockholders should consult their brokers before selling their shares of Verizon common stock in the regular way market during this time period to be sure they understand the effect of the due-bill procedures. The due-bill process is not managed, operated or controlled by Verizon.

If a Verizon stockholder sells shares of Verizon common stock in the ex-distribution market during this time period, that Verizon stockholder will be selling only his or her shares of Verizon common stock, and will retain the right to receive shares of Spinco common stock that will be converted into shares of Frontier common stock, and cash in lieu of fractional shares (if any), at the closing of the merger. It is currently expected that ex-distribution trades of Verizon common stock will settle within three business days after the closing date of the merger and that if the merger is not completed all trades in this ex-distribution market will be cancelled.

After the closing date of the merger, shares of Verizon common stock will no longer trade in the ex-distribution market, and shares of Verizon common stock that are sold in the regular way market will no longer reflect the right to receive shares of Spinco common stock that will be converted into shares of Frontier common stock, and cash in lieu of fractional shares (if any), at the closing of the merger.

Trading in Verizon common stock on the London Stock Exchange during this period is expected to be subject to the London Stock Exchange s ordinary course procedures for transactions of this type.

***Q*: Has Verizon set a record date for the distribution of shares of Spinco common stock in the spin-off?**

A: Ownership will be determined as of 5:00 p.m., Eastern time, on June 7, 2010. References to the record date for the spin-off in this information statement/prospectus refer to this date and time.

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***Q*: How may Verizon stockholders sell the shares of Frontier common stock which they are entitled to receive pursuant to the merger agreement prior to receiving those shares of Frontier common stock?**

A: It is currently expected that beginning not earlier than two business days before June 7, 2010, which is the record date for the spin-off, and continuing through the closing date of the merger (or the previous business day, if the merger closes before the opening of trading in Verizon common stock and Frontier common stock on the NYSE on the closing date), there will be two markets in Frontier common stock on the NYSE: a regular way market and a when issued market.

The regular way market will be the regular trading market for issued shares of Frontier common stock under the symbol FTR.

The when issued market will be a market for the shares of Frontier common stock that will be issued to Verizon stockholders at the closing of the merger. If a Verizon stockholder sells shares of Frontier common stock in the when issued market during this time period, that Verizon stockholder will be selling his or her right to receive shares of Frontier common stock at the closing of the merger. It is currently expected that when issued trades of Frontier common stock will settle within three business days after the closing date of the merger and that if the merger is not completed, all trades in this when issued market will be cancelled. After the closing date of the merger, shares of Frontier common stock will no longer trade in this when issued market.

***Q*: How can Verizon stockholders sell their shares of Frontier common stock after the distribution?**

A. Verizon stockholders who are record holders of shares of Frontier common stock after the distribution date may request, if they choose to do so, that the Frontier transfer agent either sell their book-entry shares or send electronically all or a portion of their book-entry shares to a broker for a sale.

In the case of Verizon stockholders who hold their shares of Frontier common stock through a brokerage account, book-entry shares can be moved to or from the stockholders brokerage accounts electronically through Frontier s transfer agent s direct registration system. Verizon stockholders who hold their shares through a brokerage account should contact their brokers for more information.

***Q*. In what ways will being a stockholder of both Verizon and the combined company differ from being a stockholder of Verizon?**

A. Following the spin-off and the merger, Verizon stockholders will continue to own all of their shares of Verizon common stock. Their rights as Verizon stockholders will not change, except that their shares of Verizon common stock will represent an interest in Verizon that no longer includes the ownership and operation of the Spinco business. Verizon stockholders will also separately own stock of the combined company, which will include the combined business operations of Frontier and Spinco.

The combined company s business will differ in several important ways from that of Verizon:

The combined company s business will focus on providing a broad array of communications services to business and residential customers in the markets currently served by Frontier and the Spinco business, while Verizon will focus on providing wireless voice and data products and services, and converged communications, information and entertainment services over its advanced fiber-optic network in the United States, as well as expansive end-to-end global Internet Protocol (IP) networks to business and government customers around the world;

The combined company will be significantly smaller than Verizon; and

Although Frontier expects the combined company to obtain an investment grade credit rating in the future, immediately after the closing of the merger the combined company is expected to have a higher amount of indebtedness relative to its market capitalization than Verizon, and may be subject to higher financing costs and more restrictive debt covenants than Verizon.

For a more complete description of the characteristics of the combined company s business, see Description of the Business of the Combined Company.

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***Q*: Will the spin-off and the merger affect employees and former employees of Verizon who hold Verizon stock options and other stock-based awards?**

A: Yes. Pursuant to the terms of the plans under which those Verizon stock options and other stock-based awards were issued, Verizon expects to adjust the exercise price of and number of shares of Verizon stock underlying the outstanding options to take into account any decrease in the value of Verizon common stock immediately following the spin-off and the merger. Also, holders of Verizon restricted stock units and Verizon performance stock units will receive additional units equivalent to the cash value of the Frontier common stock that they would have received with respect to each hypothetical share of Verizon common stock held in respect of those units. See The Transactions Effects of the Merger and Spin-Off on Verizon Stock Options and Other Verizon Stock-Based Awards.

***Q*: How will shares of Frontier common stock be distributed to Verizon stockholders?**

A: Holders of Verizon common stock on the record date for the spin-off will receive shares of Frontier common stock in book-entry form. Record stockholders will receive additional information from Frontier s transfer agent shortly after the distribution date. Beneficial holders will receive information from their brokerage firms or other nominees.

***Q*: Who is the transfer agent and the distribution agent?**

A: Computershare Trust Company, N.A. is the current transfer agent for shares of Verizon common stock and for shares of Frontier common stock, and it will also serve as the distribution agent for the shares of Frontier common stock to be distributed to Verizon stockholders following the spin-off and the merger. Any questions regarding the distribution of shares of Frontier common stock to Verizon stockholders or the ownership of Frontier common stock following the distribution should be directed to Computershare Trust Company, N.A. at (877) 770-0496. Holders of Verizon common stock who hold their shares through a brokerage account should contact their brokers with any questions.

***Q:* Will Verizon stockholders who currently participate in the full reinvestment option contained in the Verizon Communications Direct Invest plan automatically be enrolled in Frontier s dividend reinvestment plan?**

A: Yes. A Verizon stockholder who currently participates in the full reinvestment option contained in the Verizon Communications Direct Invest plan, which is a direct stock purchase and share ownership plan for holders of Verizon common stock, will have the account holding the shares of Frontier common stock that he or she receives in the merger automatically enrolled in Computershare CIP, a direct stock purchase and dividend reinvestment plan for Frontier common stock. Computershare CIP is sponsored by Computershare Trust Company, N.A. and not by Frontier. Verizon stockholders who do not wish to participate in Computershare CIP with respect to the shares of Frontier common stock that they will receive in the merger should notify Computershare Trust Company, N.A. at the telephone number specified in the previous paragraph immediately following the merger. A Verizon stockholder who participates in the Verizon Communications Direct Invest Plan with respect to only some of his or her shares of Verizon common stock will not be automatically enrolled in Computershare CIP following the merger with respect the shares of Frontier common stock that he or she receives in the merger.

***Q:* Are Verizon stockholders required to do anything?**

A: Verizon stockholders are not required to take any action to approve the spin-off or the merger. However, Verizon stockholders should carefully read this information statement/prospectus, which contains important information about the spin-off, the merger, Spinco, Frontier and the combined company. After the merger, Frontier will mail to holders of Verizon common stock who are entitled to receive shares of Frontier

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common stock book-entry statements evidencing their ownership of Frontier common stock, cash payments in lieu of fractional shares (if any) and related tax information, and other information regarding their receipt of Frontier common stock.

VERIZON STOCKHOLDERS WILL NOT BE REQUIRED TO SURRENDER THEIR SHARES OF VERIZON COMMON STOCK IN THE SPIN-OFF OR THE MERGER AND THEY SHOULD NOT RETURN THEIR VERIZON STOCK CERTIFICATES. THE SPIN-OFF AND THE MERGER WILL NOT RESULT IN ANY CHANGE IN VERIZON STOCKHOLDERS OWNERSHIP OF VERIZON COMMON STOCK FOLLOWING THE MERGER.

Q: **How will the rights of stockholders of Frontier and Verizon change after the merger?**

A: The rights of stockholders of Frontier will not change as a result of the merger. Except for the amendment of Frontier s restated certificate of incorporation to increase the number of authorized shares of Frontier common stock, which was approved by Frontier s stockholders, Frontier does not expect to further amend its restated certificate of incorporation or its by-laws in connection with the merger. The rights of stockholders of Verizon will also remain the same as prior to the merger, except that their shares of Verizon common stock will represent an interest in Verizon that no longer reflects the ownership and operation of the Spinco business, and stockholders of Verizon will also receive shares of Frontier common stock and cash paid in lieu of fractional shares (if any) in the merger. See Description of Capital Stock of Frontier and the Combined Company.

Q: **What will Frontier s dividend policy be following the merger?**

A: The amount and timing of dividends payable on Frontier s common stock are within the sole discretion of its board of directors. Frontier currently pays an annual cash dividend of $1.00 per share of Frontier common stock, subject to applicable law and agreements governing Frontier s indebtedness and within the sole discretion of the Frontier board. After the closing of the merger, Frontier intends to pay an annual cash dividend of $0.75 per share of Frontier common stock, subject to applicable law and agreements governing the combined company s indebtedness and within the sole discretion of the Frontier board. Frontier believes that this dividend policy will allow the combined company to invest in its markets, including extending its broadband capacity in the Spinco territory over the next few years. See The Transactions Dividend Policy of Frontier and the Combined Company.

Q: **Will Frontier pay a dividend for the quarter in which the merger is completed?**

A: Yes. Unless the closing date of the merger occurs on the first day of a fiscal quarter, Frontier intends to pay a pro-rated dividend for the quarter in which the merger is completed to Frontier stockholders of record as of the close of business on the business day immediately preceding the closing date of the merger based on its current policy of paying dividends on each share of its common stock at a rate of $0.25 per share per quarter. The pro-rated dividend would be payable for the period from the first day of the fiscal quarter in which the closing date of the merger occurs through and including the day immediately preceding the closing date of the merger. Subject to the satisfaction of closing conditions in the merger agreement, Frontier and Verizon expect the closing date of the merger to occur on July 1, 2010. If a pro-rated dividend is paid, Verizon stockholders who receive shares of Frontier common stock as a result of the merger will not be entitled to receive this pro-rated dividend in respect of the shares received in the merger. In addition, unless the closing date of the merger occurs on the first day of a fiscal quarter, Frontier intends to pay a pro-rated dividend at a rate of $0.1875 per share per quarter for the period beginning on the closing date of the merger through and including the last day of the fiscal quarter in which the closing of the merger occurs. Existing Frontier stockholders and Verizon stockholders who receive shares of Frontier common stock as a result of the merger and who continue to hold the shares on the relevant record date would be entitled to receive this pro-rated dividend. However, as noted above, no pro-rated dividend will be paid in the event that the closing of the merger occurs on the first day of a fiscal quarter.

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Q: **Who will serve on the board of directors of the combined company?**

A: Currently, the Frontier board (which will become the board of directors of the combined company) consists of ten directors plus two vacancies. All of Frontier s current directors will continue to serve on Frontier s board after the merger, with the exception of Ms. Lawton Fitt, who has agreed to resign immediately prior to the merger. Frontier expects that Mary Agnes Wilderotter, Frontier s current Chairman of the Board of Directors, President and Chief Executive Officer, will continue to serve in such roles with the combined company. On July 6, 2010, or if the merger were to close later, the day immediately prior to the merger, three nominees designated by Verizon will be elected to fill vacancies on Frontier s board. Following such elections, Frontier s board will consist of twelve directors. Verizon has designated Edward Fraioli, Pamela D.A. Reeve and Mark Shapiro to be elected to the board of directors of the combined company in connection with the closing of the merger.

Q: **Will Frontier s current senior management team manage the business of the combined company following the merger?**

A: Yes. Frontier s senior management team will continue to manage the business of the combined company after the merger. In addition, Frontier expects to supplement Frontier s current senior management team with members of Verizon s regional management team who currently manage the Spinco business. See Management of the Combined Company.

Q: **What will be the indebtedness of the combined company immediately following completion of the spin-off and merger?**

A: By virtue of the merger, the combined company will have approximately $3.5 billion of additional indebtedness compared to Frontier s indebtedness immediately prior to the merger. This additional indebtedness will consist primarily of $3.2 billion of special cash payment financing and $250 million of distribution date indebtedness. The combined company will also continue to be obligated in respect of Frontier s indebtedness existing at the time of the merger. Based upon Frontier s outstanding indebtedness as of March 31, 2010 of approximately $4.8 billion, Frontier expects that, immediately following the merger, the combined company will have approximately $8.3 billion in total debt.

Q: **Will there be a post-closing working capital adjustment?**

A: Pursuant to the distribution agreement, Spinco is required to have, at the closing of the merger, defined current assets in an amount that is at least equal to the amount of defined current liabilities as of such time, referred to as the distribution date working capital. If the distribution date working capital of Spinco exceeds zero, no payment will be made by either party with respect to such excess. If the distribution date working capital of Spinco is less than zero, Verizon will pay to the combined company an amount equal to the full amount of the deficit. In the event that the combined company disagrees with Verizon s calculation of the distribution date working capital, the combined company may dispute that calculation if the amount in dispute exceeds $250,000.

Q: **What are the material tax consequences to Verizon stockholders resulting from the spin-off and the merger?**

A: Verizon stockholders are not expected to recognize any gain or loss for U.S. federal income tax purposes as a result of the spin-off or the merger, except for any gain or loss attributable to the receipt of cash in lieu of a fractional share of Frontier common stock. The material U.S. federal income tax consequences of the spin-off and the merger are described in more detail under Material United States Federal Income Tax Consequences of the Spin-Off and the Merger.

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Q: **Are there risks associated with the merger?**

A: Yes. The combined company may not achieve the expected benefits of the merger because of the risks and uncertainties discussed in the sections titled Risk Factors and Cautionary Statement Regarding Forward-Looking Statements. Those risks include, among other things, risks relating to the uncertainty that the combined company will fully realize the anticipated growth opportunities and cost synergies from the merger and uncertainties relating to the performance of the combined company following the completion of the merger.

Q: **Does Frontier have to pay anything to Verizon if the merger agreement is terminated?**

A: Depending on the reasons for termination of the merger agreement, Frontier may have to pay Verizon a termination fee of $80 million. For a discussion of the circumstances under which the termination fee is payable by Frontier to Verizon, see The Transaction Agreements The Merger Agreement Termination Fee Payable in Certain Circumstances.

Q: **Can Verizon or Frontier stockholders demand appraisal of their shares?**

A: No. Neither Verizon nor Frontier stockholders have appraisal rights under Delaware law in connection with the spin-off or the merger.

Q: **When will the merger be completed?**

A: Subject to the satisfaction of the closing conditions in the merger agreement, Frontier and Verizon expect the merger to close on July 1, 2010. For a discussion of the conditions to the merger, see The Transaction Agreements The Merger Agreement Conditions to the Completion of the Merger.

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SUMMARY

This summary highlights selected information from this information statement/prospectus and may not contain all of the information that is important to you. To understand the transactions fully and for a more complete description of the terms of the spin-off and the merger, please carefully read this entire information statement/prospectus and the other documents referred to in this information statement/prospectus. See also Where You Can Find Additional Information.

This information statement/prospectus is:

- an information statement of Spinco relating to the distribution in the spin-off of shares of its common stock to the distribution agent for the benefit of Verizon stockholders; and

- a prospectus of Frontier relating to the issuance of shares of Frontier common stock to Verizon stockholders in connection with the merger.

The Companies

Frontier Communications Corporation

Frontier is a communications company providing services to rural areas and small and medium-sized towns and cities. Frontier generated revenues of approximately $2.1 billion for the fiscal year ended December 31, 2009 and approximately $519.8 million for the three months ended March 31, 2010. Frontier operated in 24 states with approximately 2,083,000 access lines, 644,000 Internet subscribers and 176,000 video subscribers as of March 31, 2010.

Incorporated in November 1935, Frontier is the sixth largest incumbent local exchange carrier (ILEC) in the United States based on number of access lines. Frontier is typically the leading incumbent carrier in the markets it serves and provides the last mile of communications services to residential and business customers in these markets.

From May 2000 until July 31, 2008, Frontier was named Citizens Communications Company.

Spinco

The Spinco business had approximately 4,108,000 access lines as of March 31, 2010. Verizon s Separate Telephone Operations generated revenues of approximately $4.1 billion for the year ended December 31, 2009 and approximately $964 million for the three months ended March 31, 2010.

Verizon s Separate Telephone Operations financial information is included elsewhere in this information statement/prospectus before taking into account any of the pro forma adjustments detailed in Unaudited Pro Forma Condensed Combined Financial Information. This financial information, together with the pro forma adjustments detailed in Unaudited Pro Forma Condensed Combined Financial Information, reflects the operations that will comprise the Spinco business in connection with the spin-off.

Pursuant to the distribution agreement, Verizon will contribute to Spinco defined assets and liabilities of its local exchange business and related landline activities in the Spinco territory, including Internet access and long distance services and broadband video provided to designated customers in the Spinco territory. This information statement/prospectus describes Spinco as if it had the assets, liabilities and customers that will be transferred to it prior to completion of the spin-off and the merger for all periods and dates presented. The Spinco business consists of local exchange service, designated intrastate and interstate long distance service, network access service, Internet access service, enhanced voice and data services, digital subscriber line services, referred to as

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DSL, fiber-to-the-premises voice, broadband and video services, wholesale services, operator services, directory assistance services, customer service to end users, and, in connection with the foregoing, repairs, billing and collections, as well as other specified activities of Verizon in the Spinco territory. The conveyed assets will specifically include designated fiber-to-the-premises network elements and customer premises equipment at fiber-to-the-premises subscriber locations in the states of Indiana, Oregon and Washington and specified related transmission facilities.

The Combined Company

The combined company is expected to be the nation s largest communications services provider focused on rural areas and small and medium-sized towns and cities, and the nation s fifth largest incumbent local exchange carrier, with approximately 6.2 million access lines, 7.7 million voice and broadband connections and 13,800 employees in 27 states on a pro forma basis as of March 31, 2010. The combined company will offer voice, data and video services to customers in its expanded geographic footprint. Assuming the merger had occurred on January 1, 2009, the combined company s revenues on a pro forma basis would have been approximately $6.1 billion for the year ended December 31, 2009 and approximately $1.5 billion for the three months ended March 31, 2010.

The Transactions

The Spin-Off (See The Transactions The Spin-Off beginning on page 40)

As part of the spin-off, pursuant to the distribution agreement, Verizon will, pursuant to a series of restructuring transactions prior to the spin-off (collectively referred to as the contribution) contribute to Spinco and its subsidiaries defined assets and liabilities of the local exchange business and related landline activities of Verizon in the Spinco territory, including Internet access and long distance services and broadband video provided to designated customers in the Spinco territory. In connection with the contribution, Verizon will receive from Spinco $3.333 billion in aggregate value in the form of:

- a special cash payment of $3,083 million; and
- the Verizon debt reduction in the amount of $250 million.

Also in connection with the contribution, Spinco will issue additional shares of Spinco common stock to Verizon, which will be distributed in the spin-off as described below.

After the contribution and immediately prior to the merger, Verizon will spin off Spinco by distributing all of the shares of Spinco common stock to the distribution agent to be held collectively for the benefit of Verizon stockholders, which transactions are referred to collectively as the distribution. Spinco will then merge with and into Frontier, and the shares of Spinco common stock will be immediately converted into the number of shares of Frontier common stock that Verizon stockholders will be entitled to receive in the merger. The distribution agent will then distribute these shares of Frontier common stock and cash in lieu of fractional shares to Verizon stockholders on a pro rata basis in accordance with the terms of the merger agreement.

The Merger (See The Transactions The Merger beginning on page 41)

In the merger, Spinco will merge with and into Frontier in accordance with the terms of the merger agreement and, following completion of the merger, the separate existence of Spinco will cease. Frontier will survive the merger as the combined company and will hold and conduct the combined business operations of Frontier and Spinco.

Verizon stockholders will be entitled to receive a number of shares of common stock of Frontier, as the combined company, to be determined based on the calculation set forth in The Transactions Calculation of

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Merger Consideration. Verizon stockholders will receive a cash payment in lieu of any fractional shares of Frontier common stock that they would otherwise receive. Verizon stockholders will not be required to pay for any of the shares of Frontier common stock they receive and will also retain all of their shares of Verizon common stock. Existing shares of Frontier common stock will remain outstanding.

Frontier, Spinco and Verizon stockholders will not be entitled to exercise appraisal rights or to demand payment for their shares in connection with the spin-off or the merger.

Approval of the Transactions

On October 27, 2009, Frontier stockholders voted to adopt the merger agreement and approve the issuance of Frontier common stock pursuant to the merger agreement. No vote by Verizon stockholders is required or is being asked for in connection with the spin-off or the merger. Verizon, as the sole stockholder of Spinco, has already approved the merger.

Opinions of Financial Advisors to Frontier (See The Transactions Opinions of Frontier s Financial Advisors beginning on page 51)

The Frontier board received an oral opinion of Evercore Group L.L.C., referred to as Evercore, on May 12, 2009, which opinion was confirmed by a written opinion dated May 12, 2009, to the effect that, as of that date and based on and subject to the assumptions made, matters considered and limitations on the scope of review undertaken by Evercore as set forth therein, the aggregate merger consideration to be delivered by Frontier in respect of the Spinco common stock pursuant to the merger agreement entered into by Verizon, Spinco and Frontier on May 13, 2009, which was prior to any subsequent amendment and is referred to as the original merger agreement, was fair, from a financial point of view, to Frontier and the holders of Frontier common stock (solely in their capacity as holders of Frontier common stock). The full text of Evercore s written opinion, which sets forth, among other things, the procedures followed, assumptions made, matters considered and limitations on the scope of review undertaken by Evercore in connection with delivering its opinion, is attached as Annex B-1 to this information statement/prospectus and is incorporated by reference in its entirety into this information statement/prospectus. The opinion of Evercore was provided to the Frontier board in connection with its evaluation of the consideration provided for in the merger and does not address the fairness of the spin-off or the merger from a financial point of view to Verizon, Spinco, or their respective stockholders or any other aspect of the proposed transactions, and does not constitute a recommendation to the recipients of this information statement/prospectus or any other person with respect to the spin-off, the merger or any other transaction. Evercore did not provide any advice or opinion to Verizon, Spinco or their respective boards of directors with respect to the spin-off, the merger or any other aspect of the proposed transactions.

The Frontier board also received an oral opinion of Citigroup Global Markets Inc., referred to as Citi, on May 12, 2009, which opinion was subsequently confirmed by a written opinion dated May 13, 2009, to the effect that, as of that date and based upon and subject to the assumptions, limitations and considerations set forth therein, the aggregate merger consideration to be delivered by Frontier in respect of the Spinco common stock pursuant to the original merger agreement was fair, from a financial point of view, to Frontier and the holders of Frontier common stock. The full text of Citi s written opinion, which sets forth the assumptions made, general procedures followed, matters considered and limits on the review undertaken by Citi in connection with its opinion, is attached as Annex B-2 to this information statement/prospectus and is incorporated by reference in its entirety into this information statement/prospectus. The opinion of Citi was provided to the Frontier board in connection with its evaluation of the consideration provided for in the merger and does not address the fairness of the spin-off or the merger from a financial point of view to Verizon, Spinco, or their respective stockholders or any other aspect of the proposed transactions, and does not constitute a recommendation to the recipients of this information statement/prospectus or any other person with respect to the spin-off, the merger or any other transaction. Citi did not provide any advice or opinion to Verizon, Spinco or their respective boards of directors with respect to the spin-off, the merger or any other aspect of the proposed transactions.

Board of Directors and Management of the Combined Company (See Management of the Combined Company beginning on page 183)

Immediately prior to the merger, the Frontier board (which will become the board of directors of the combined company) will consist of twelve directors, nine of whom will be initially designated by Frontier and three of whom will be initially designated by Verizon. However, in the event that the closing date of the merger occurs on or prior to July 6, 2010, there will be three vacancies on the Frontier board immediately prior to the merger and the three Verizon director nominees will become members of the board of directors of the combined company on July 6, 2010. If the closing date of the merger occurs after July 6, 2010, the three Verizon director nominees will become members of the board of the combined company on the day immediately prior to the merger. Verizon s director nominees may not be employees of Verizon, its affiliates or Cellco or any of its subsidiaries, and must satisfy the requirements for director independence under the rules and regulations of the SEC and the NYSE. The officers of Frontier immediately prior to the merger will continue as the officers of the combined company immediately following the merger. In addition, Frontier expects to supplement its current senior management team with members of Verizon s regional management team who currently manage the Spinco business.

Risk Factors (See Risk Factors beginning on page 22)

You should carefully consider the matters described in the section Risk Factors, as well as other information included in this information statement/prospectus and the other documents to which you have been referred.

Regulatory Matters (See The Transaction Agreements The Merger Agreement Regulatory Matters beginning on page 82)

The merger agreement provides that each of the parties to the merger agreement will use all commercially reasonable efforts to obtain all necessary actions, waivers, consents and approvals from any governmental authority, and to take all steps as may be necessary to obtain an approval or waiver from, or to avoid an action by, any governmental authority. This includes making all necessary filings and defending or contesting all actions or proceedings (subject to certain limitations).

Financing (See The Transaction Agreements The Merger Agreement Financing Matters beginning on page 85)

The gross proceeds of the notes offering (less the initial purchasers discount) will be used to make the special cash payment by Spinco to Verizon, with any such amount in excess of the special cash payment to be retained by the combined company.

Conditions (See The Transaction Agreements The Merger Agreement Conditions to the Completion of the Merger beginning on page 89)

As more fully described in this information statement/prospectus and in the merger agreement and distribution agreement, consummation of the merger is subject to the satisfaction of certain conditions, including (1) the absence of any order by a court or governmental authority enjoining or prohibiting any of the transactions, (2) the absence of any action taken by any governmental authority in connection with the transactions that would reasonably be expected to have a material adverse effect on Verizon (assuming Verizon were comparable in size to the combined company) or the combined company, (3) the continuing effectiveness of applicable regulatory consents, (4) the receipt of certain tax opinions, (5) the absence of a material adverse effect on Frontier, on Spinco or on the Spinco business, (6) the receipt by Verizon and Frontier of a solvency opinion of a nationally recognized independent valuation firm, and (7) other customary closing conditions. There can be no assurance when, or if, the conditions to the merger will be satisfied or waived, or that the merger will be completed.

Termination (See The Transaction Agreements The Merger Agreement Termination beginning on page 91)

The merger agreement may be terminated by:

(a) the mutual written consent of the parties;

(b) any of the parties if the merger is not consummated by July 31, 2010, subject to certain extension rights;

(c) any of the parties if the merger is permanently enjoined or prohibited, or if a final, non-appealable order has been entered into that would constitute a materially adverse regulatory condition;

(d) Frontier, on the one hand, or Verizon and Spinco, on the other hand, if the other party or parties breach the merger agreement in a way that would entitle the party or parties seeking to terminate the agreement not to consummate the merger, subject to the right of the breaching party or parties to cure the breach;

(e) Verizon and Spinco, if the Frontier board withdraws or adversely modifies its recommendation; or

(f) Verizon and Spinco on any date, if on that date (1) the average of the volume-weighted averages of the trading prices of the Frontier common stock for any period of 60 consecutive trading days that ended within three business days prior to that date is below $3.87 and (2) Verizon and Spinco notify Frontier in writing that they are terminating the merger agreement in accordance with this provision.

Frontier will pay to Verizon a termination fee of $80 million in the event that:

- Verizon and Spinco terminate the merger agreement under clause (e) above; or

- (1) Frontier receives a competing acquisition proposal and one of the parties terminates under clause (b) above or Verizon and Spinco terminate the merger agreement because Frontier breaches certain specified provisions of the merger agreement, and (2) within 12 months after such termination of the merger agreement, Frontier consummates a business combination transaction or enters into a definitive agreement with respect to such a transaction.

Material United States Federal Income Tax Consequences (See Material United States Federal Income Tax Consequences of the Spin-off and the Merger beginning on page 73)

Verizon stockholders are not expected to recognize any gain or loss for U.S. federal income tax purposes as a result of the spin-off or the merger, except for any gain or loss attributable to the receipt of cash in lieu of a fractional share of Frontier common stock.

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SUMMARY HISTORICAL CONSOLIDATED AND COMBINED FINANCIAL INFORMATION AND UNAUDITED PRO FORMA CONDENSED COMBINED FINANCIAL INFORMATION

Frontier

The following tables present summary historical consolidated financial and operating information of Frontier as of the dates and for the periods indicated. The summary historical consolidated financial information of Frontier as of March 31, 2010 and for the three months ended March 31, 2010 and 2009 have been derived from the unaudited interim consolidated financial statements of Frontier included elsewhere in this information statement/prospectus. The summary historical consolidated financial information of Frontier as of December 31, 2009 and 2008 and for each of the years in the three-year period ended December 31, 2009 is derived from the audited historical consolidated financial statements of Frontier included elsewhere in this information statement/prospectus. The summary historical consolidated financial information of Frontier as of December 31, 2007, 2006 and 2005 and for each of the years in the two-year period ended December 31, 2006 is derived from the audited historical consolidated financial statements of Frontier not included in this information statement/prospectus. The operating data of Frontier below is unaudited for all periods. The operating results of Frontier for the three months ended March 31, 2010 and for the year ended December 31, 2009 are not necessarily indicative of the results to be expected for any future periods.

This information is only a summary and should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and related notes of Frontier referred to above.

	Three months ended March 31,		Year ended December 31,			
(In thousands)	**2010**	**2009**	**2009**	**2008**	**2007**	**2006**
Research and development	6,561	5,545	21,665	17,538		
Selling, general and administrative	34,762	29,316	100,866	86,382		
Total operating expenses	41,323	34,861	122,531	103,920		
Income from operations	10,717	11,226	24,244	17,292		
Interest and other income (expense), net	25	34	(134)	57		
Income before provision for income taxes	10,742	11,260	24,110	17,349		
Provision for income taxes	2,987	4,340	6,954	6,703		
Net income	$ 7,755	$ 6,920	$ 17,156	$ 10,646		
Net income per share-basic	$ 0.22	$ 0.21	$ 0.50	$ 0.32		
Net income per share-diluted	$ 0.21	$ 0.20	$ 0.48	$ 0.31		
Weighted average shares outstanding:						
Basic	35,133	33,193	34,499	33,316		
Diluted	36,190	34,068	35,466	34,241		

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 September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income	$7,755	$6,920	$17,156	$10,646
Other comprehensive income (loss) and reclassification adjustments:				
Unrealized holding losses on securities arising during the period	—	—	—	(1)
Changes in fair value of foreign currency forward hedges	—	—	(65)	65
Foreign currency translation adjustment	217	70	21	54
Other comprehensive income (loss)	217	70	(44)	118
Comprehensive income	$7,972	$6,990	$17,112	$10,764

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)

	Nine Months Ended September 30, 2013	2012
Cash flows from operating activities:		
Net income	$17,156	$10,646
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,732	9,247
Loss on disposal of fixed assets	289	28
Impairment of software development costs	1,759	—
Provision for receivable allowance	110	410
Share-based compensation expense	8,387	6,781
Income tax benefits from employee stock plans	1,707	1,638
Excess tax benefits from employee stock plans	(2,827)	(2,336)
Provision for excess and obsolete inventories	911	509
Deferred income taxes	(737)	(1,084)
Changes in operating assets and liabilities:		
Accounts receivable, net	(9,004)	(7,103)
Inventories	(4,713)	2,924
Prepaid expenses	(1,661)	(3,453)
Other current assets	(394)	921
Net investment in sales-type leases	1,313	(1,493)
Other assets	307	(13)
Accounts payable	6,462	2,131
Accrued compensation	1,263	802
Accrued liabilities	2,031	(1,719)
Deferred service revenue	(403)	2,117
Deferred gross profit	4,434	5,377
Other long-term liabilities	615	1,147
Net cash provided by operating activities	40,737	27,477
Cash flows from investing activities:		
Maturities of short-term investments	—	8,122
Acquisition of intangible assets and intellectual property	(225)	(303)
Software development for external use	(5,694)	(3,118)
Purchases of property and equipment	(7,817)	(9,560)
Business acquisition, net of cash acquired	—	(156,312)
Net cash used in investing activities	(13,736)	(161,171)
Cash flows from financing activities:		
Proceeds from issuance of common stock under employee stock purchase and stock option plans	24,020	6,777
Stock repurchases	—	(12,363)
Excess tax benefits from employee stock plans	2,827	2,336
Net cash provided by (used in) from financing activities	26,847	(3,250)
Effect of exchange rate changes on cash and cash equivalents	29	—
Net increase (decrease) in cash and cash equivalents	53,877	(136,944)

Cash and cash equivalents at beginning of period	62,313	191,762
Cash and cash equivalents at end of period	$116,190	$54,818
Acquisition consideration accrued but not paid	$—	$(1,482)

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 now serve both the acute care and non-acute care markets. 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 September 30, 2013, the results of their operations and comprehensive income for the three and nine months ended September 30, 2013 and 2012 and their cash flows for the nine months ended September 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 three and nine months ended September 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; and
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 September 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 September 30, 2013 and December 31, 2012, we held $64.8 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 September 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 in accordance with ASC 280, Segment Reporting. Beginning with the acquisition of MTS in May 2012, we have organized our business into two operating business segments: Acute Care, which includes primarily products and services sold to hospital customers, and Non-Acute Care, which includes primarily 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.

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.

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- 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 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-

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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 September 30, 2013 and 2012, we transferred non-recourse accounts receivable totaling $7.2 million and $14.6 million, respectively, which approximated fair value, to third-party leasing companies. During the nine months ended September 30, 2013 and 2012, we transferred non-recourse accounts receivable totaling $28.1 million and $42.5 million, respectively, which approximated fair value, to third-party leasing companies. At September 30, 2013 and December 31, 2012, accounts receivable included $0.5 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 nine months ended September 30, 2013. Additionally, there was no single customer accounting for 10% or more of accounts receivable at September 30, 2013 or December 31, 2012. At September 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 $1.5 million and $1.2 million for the three months ended September 30, 2013 and 2012, respectively. Shipping and handling expenses totaled $4.5 million and $2.7 million for the nine months ended September 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 September 30, 2013 and 2012 totaled approximately $8.6 million and $6.3 million, respectively. Purchases from this supplier for the nine months ended September 30, 2013 and 2012 totaled approximately $22.5 million and $17.8 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. 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.

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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 38.1% and 41.5% for the nine months ended September 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 ASU 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 1,178,755 and 2,067,273 shares from the calculations of diluted net income per share for the nine months ended September 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 September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Basic:				
Net income	$7,755	$6,920	$17,156	$10,646
Weighted average shares outstanding — basic	35,133	33,193	34,499	33,316
Net income per share — basic	$0.22	$0.21	$0.50	$0.32
Diluted:				
Net income	$7,755	$6,920	$17,156	$10,646
Weighted average shares outstanding — basic	35,133	33,193	34,499	33,316
Add: Dilutive effect of employee stock plans	1,057	875	967	925
Weighted average shares outstanding — diluted	36,190	34,068	35,466	34,241
Net income per share — diluted	$0.21	$0.20	$0.48	$0.31

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

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

	September 30, 2013					
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash / Cash Equivalents	Security Classification
Cash	$51,415	$—	$—	$51,415	$51,415	N/A
Money market fund	64,775	—	—	64,775	64,775	Available for sale
Total cash and cash equivalents	$116,190	$—	$—	$116,190	$116,190	

c	December 31, 2012					
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash / Cash Equivalents	Security Classification
Cash	$23,422	$—	$—	$23,422	$23,422	N/A
Money market fund	38,892	—	1	38,891	38,891	Available for sale
Total cash and cash equivalents	$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 September 30, 2013				
Money market fund	$64,775	$—	$—	$64,775
Total	$64,775	$—	$—	$64,775
At December 31, 2012				
Money market fund	$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):

	September 30, 2013	December 31, 2012
Raw materials	$11,120	$9,994
Work in process	963	385
Finished goods	18,622	16,524
Total	$30,705	$26,903

Note 5. Property and Equipment

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

	September 30, 2013	December 31, 2012
Equipment	$35,483	$32,528
Furniture and fixtures	5,149	5,126
Leasehold improvements	7,356	6,992
Purchased software	19,800	19,870
Capital in process	3,491	2,693
	71,279	67,209
Accumulated depreciation and amortization	(37,787)	(33,102)
Property and equipment, net	$33,492	$34,107

Depreciation and amortization of property and equipment totaled approximately $2.6 million and $2.2 million for the three months ended September 30, 2013 and 2012, respectively. Depreciation and amortization of property and equipment totaled approximately $8.2 million and $5.7 million for the nine months ended September 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):

	September 30, 2013	December 31, 2012
Net minimum lease payments to be received	$18,788	$19,665
Less unearned interest income portion	1,157	1,205
Net investment in sales-type leases	17,631	18,460
Less current portion(1)	5,233	5,232
Non-current net investment in sales-type leases(2)	$12,398	$13,228

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

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

2013 (remaining three months)	$1,640
2014	5,495
2015	4,536
2016	3,341
2017	2,603
Thereafter	1,173
Total	$18,788

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 September 30, 2013:			
Accounts individually evaluated for impairment	$ 22	$22	$—
Accounts collectively evaluated for impairment	152	17,783	17,631
Ending balances: September 30, 2013	$ 174	$17,805	$17,631
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 nine months ended September 30, 2013 and 2012 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Allowance for credit losses, beginning of period	$184	$659	$607	$284
Current period provision	15	4	34	426
Direct write-downs charged against the allowance	—	—	(413)	—
Recoveries of amounts previously charged off	(25)	(26)	(54)	(73)
Allowance for credit losses, end of period	$174	$637	$174	$637

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 unit, which is the same for our operating segments, for the nine months ended September 30, 2013 consists of the following (in thousands):

	Goodwill at December 31, 2012	Adjustments to Goodwill	Goodwill at September 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 our 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 September 30, 2013 or December 31, 2012. Finite-life intangible assets consist of the following (in thousands):

	September 30, 2013			December 31, 2012			
	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	$4,698	$50,032	$54,730	$3,081	$51,649	5-30 years
Acquired technology	27,580	2,230	25,350	27,580	1,128	26,452	3-20 years
Patents	1,363	244	1,119	1,217	259	958	20 years
Trade name	6,890	861	6,029	6,890	414	6,476	3-12 years
Non-compete agreements	60	60	—	60	45	15	3 years
Total finite-lived intangibles	$90,623	$8,093	$82,530	$90,477	$4,927	$85,550	

Amortization expense totaled $1.1 million and $1.1 million for the three months ended September 30, 2013 and 2012, respectively. Amortization expense totaled $3.2 million and $1.8 million for the nine months ended September 30, 2013 and 2012, respectively. The amortization of acquired technology is included within product cost of sales; other acquired intangibles are usually amortized within selling, general and administrative expenses.

Estimated annual expected amortization expense of the finite-lived intangible assets at September 30, 2013 was as follows (in thousands):

2013 (remaining three months)	$1,059
2014	4,229
2015	4,204
2016	3,854
2017	3,818
2018	3,711
Thereafter	61,655
Total	$82,530

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Note 8. Accrued Liabilities

Accrued liabilities consist of the following (in thousands):

	September 30, 2013	December 31, 2012
Rebates and lease buyouts	$3,379	$3,179
Advance payments from customers	4,272	2,829
Accrued Group Purchasing Organization (GPO) fees	2,492	2,278
Technology license purchase obligation, current portion	1,500	1,750
Taxes payable (receivable)	774	555
Other	1,602	1,397
Total	$14,019	$11,988

Note 9. Deferred Gross Profit

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

	September 30, 2013	December 31, 2012
Sales of medication and supply dispensing systems and packaging equipment, which have been delivered and invoiced but not yet installed	$40,919	$30,138
Cost of revenues, excluding installation costs	(15,713)	(9,366)
Deferred gross profit	$25,206	$20,772

Note 10. Commitments

At September 30, 2013, the minimum payments under our operating leases for each of the five succeeding fiscal years were as follows (in thousands):

2013 (remaining three months)	$1,462
2014	5,722
2015	5,476
2016	5,150
2017	4,468
2018	4,298
Thereafter	16,600
Total	$43,176

In October 2011, we entered into a lease agreement for approximately 100,000 square feet of office space. Pursuant to the lease agreement, the landlord constructed a single, three-story building of rentable space in Mountain View, California which we now lease and which serves as our headquarters. The term of the lease agreement, which commenced in November 2012, is for a period of 10 years, with a base lease commitment of approximately $40.0 million. We have two options to extend the term of the lease agreement at market rates. Each extension is for an additional 60 month term.

In March 2012, we entered into a lease agreement for approximately 46,000 square feet of manufacturing, distribution and office space located in Milpitas, California which commenced in October, 2012. The term of the lease agreement is for a period of 60 months, with a base lease commitment of approximately $1.8 million and a single 60 month extension option.

In connection with the acquisition of MTS, we assumed responsibility for 132,500 square feet of manufacturing, warehousing and office space in St. Petersburg, Florida. The remaining term of the original lease agreement was for a period of 12 years, which expires in September 2016 and at the time of the MTS acquisition, with a base lease commitment of approximately $3.9 million. We have two options to extend the term of the lease agreement at market rates. Each extension is for an additional 60 month term.

In Leeds, United Kingdom, we lease an office and distribution center of approximately 16,500 square feet. The remaining term of the original ten year lease agreement is through June 8, 2021, with no extension options. The base lease

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commitment at the time of the MTS acquisition, converted from British Pounds at the conversion rate then in effect, was approximately $1.2 million.

We also have smaller rented offices in Strongsville, Ohio, Nashville, Tennessee, Waukegan, Illinois, the United Arab Emirates, the People's Republic of China and the Federal Republic of Germany.

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 $7.5 million as of September 30, 2013.

At September 30, 2013, we have recorded $4.7 million for uncertain tax positions under long term liabilities in accordance with GAAP, summarized under Note 1, "Organization and Summary of Significant Accounting Policies." As these liabilities do not reflect actual tax assessments, the timing and amount of payments we might be required to make will depend upon a number of factors. Accordingly, as the timing and amount of payment cannot be estimated, we do not present this in a commitments table.

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 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 United States District Court for the District of New Jersey 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. Omnicell is currently awaiting a decision from the court and intends to defend the matter vigorously.

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 have not recorded any accrual for contingent liabilities associated with the legal proceedings described above based on our belief that any potential loss, while reasonably possible, is not probable. Further, any possible range of loss in these matters cannot be reasonably estimated at this time. 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

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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.
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 September 30, 2013 or December 31, 2012.
Note 12. Stockholders' Equity

Treasury Stock

2008 Stock Repurchase Program

In February 2008, our Board of Directors authorized a stock repurchase program (the "2008 Repurchase Program") for the repurchase of up to $90.0 million of our common stock. The timing, price and volume of the repurchases have been based on market conditions, relevant securities laws and other factors.

There were no shares repurchased during both the three and nine months ended September 30, 2013 under the 2008 Repurchase Program. During the three months ended September 30, 2012, we repurchased 393,031 shares through the 2008 Repurchase Program at an average cost of $13.49 per share, including commissions, compared to 505,137 shares repurchased in the three months ended June 30, 2012 at an average cost of $13.98 per share, including commissions. For the nine months ended September 30, 2012, we repurchased 898,168 shares at an average cost of 13.76 per share, including commissions.

From the inception of the 2008 Repurchase Program in February 2008 through September 30, 2013, we have repurchased a total of 5,853,975 shares at an average cost of $15.37 per share through open market purchases. As of September 30, 2013, we have completed the 2008 Repurchase Program having repurchased $90.0 million of our common stock.

2012 Stock Repurchase Program

On August 1, 2012, our Board of Directors established a new 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 stock repurchase program does not obligate Omnicell to repurchase any specific number of shares, and Omnicell may terminate or suspend the repurchase program at any time.

Through September 30, 2013, we have not repurchased any shares through the 2012 Repurchase Program.

Note 13. Stock Option Plans and Share-Based Compensation

Stock Option Plans
Description of Share-Based Plans

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Equity Incentive Plan

On May 19, 2009, at our 2009 Annual Meeting of Stockholders (the "2009 Annual Meeting") our stockholders approved the Omnicell, Inc. 2009 Equity Incentive Plan (the "2009 Plan") which authorized 2,100,000 shares to be issued. The 2009 Plan provides for the issuance of incentive stock options, non-statutory stock options, stock appreciation rights, restricted stock awards, restricted stock unit awards, performance stock awards, performance cash awards and other stock awards to our employees, directors and consultants.

The 2009 Plan succeeded the 1999 Equity Incentive Plan, as amended, the 2003 Equity Incentive Plan, as amended, and the 2004 Equity Incentive Plan (collectively, the "Prior Plans"). No additional awards will be granted under any of the Prior Plans; however, all outstanding stock awards granted under the Prior Plans continue to be subject to the terms and conditions as set forth in the agreements evidencing such stock awards. For purposes of determining future common shares available for grant, for each share granted as a full-value award, including restricted stock and restricted stock units ("RSUs") performance stock awards, the shares available for grant were reduced by 1.4 shares. Equity awards granted as stock options and stock appreciation rights reduce the shares available for grant by one share.

On December 16, 2010, at a Special Meeting of Stockholders, our stockholders approved an amendment to increase the number of shares of common stock authorized for issuance under the 2009 Plan by 2,600,000 shares and to provide that the number of common stock shares available for issuance under the 2009 Plan be reduced by 1.8 shares for each share granted as a full-value award granted on and after October 1, 2010. For each share granted as a full-value award granted prior to October 1, 2010, future shares available for grants under the 2009 Plan were reduced by 1.4 shares. Awards granted as stock options and stock appreciation rights continue to reduce the number of shares available for issuance under the 2009 Plan on a one-for-one basis. On May 21, 2013, at our Annual Meeting of Stockholders, our stockholders approved an amendment to increase the number of shares of common stock authorized for issuance under the 2009 Plan by 2,500,000 shares.

Options granted under the 2009 Plan generally become exercisable over periods of up to 4 years , generally with one-fourth of the shares vesting one year from the vesting commencement date with respect to initial grants, and the remaining shares vesting in 36 equal monthly installments thereafter; however our board of directors may impose different vesting terms at its discretion on any award. Options under the 2009 Plan generally expire 10 years from the date of grant. We also grant both restricted stock and restricted stock units to participants under the 2009 Plan. The Board of Directors determines the award amount, the vesting provisions and the expiration period (not to exceed ten years) for each grant. Grants of restricted stock to non-employee directors are granted on the date of our annual meeting of stockholders and vest in full on the date of our next annual meeting of stockholders, provided such non-employee director remains a director on such date. The fair value of the stock on the date of issuance is amortized to expense from the date of grant to the date of vesting. RSUs granted to employees generally vest over a period of four years and are expensed ratably on a straight-line basis over the vesting period. We consider the dilutive impact of options, restricted stock and restricted stock units in our diluted net income per share calculation.

The Board of Directors shall administer the 2009 Plan unless and until the Board of Directors delegates administration to a committee. Our Board of Directors has delegated administration of the 2009 Plan to the Compensation Committee of the Board of Directors and the 2009 Plan is generally administered by such committee. The Board of Directors may suspend or terminate the 2009 Plan at any time. The Board of Directors may also amend the 2009 Plan at any time or from time to time. However, no amendment will be effective unless approved by our stockholders after its adoption by our Board of Directors to the extent stockholder approval is necessary to satisfy the applicable listing requirements of NASDAQ.

If we sell, lease or dispose of all or substantially all of our assets, or we are acquired pursuant to a merger or consolidation, then the surviving entity may assume or substitute all outstanding awards under the 2009 Plan. If the surviving entity does not assume or substitute these awards, then generally the stock awards will immediately and fully vest.

At September 30, 2013, a total of 3,353,608 shares of common stock were reserved for future issuance under the 2009 Plan. At September 30, 2013, $6.0 million of total unrecognized compensation cost related to non-vested stock options was expected to be recognized over a weighted average period of 2.6 years.

A summary of aggregate option activity for the nine months ended September 30, 2013 is presented below:

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Options:	Number of Shares	Weighted-Average Exercise Price
	(in thousands)	
Outstanding at December 31, 2012	4,470	$14.06
Granted	296	$18.10
Exercised	(1,450)	$12.59
Forfeited	(75)	$14.40
Expired	(56)	$15.68
Outstanding at September 30, 2013	3,185	$15.07
Exercisable at September 30, 2013	2,186	$14.85

Restricted Stock and Time-based Restricted Stock Units

The non-employee members of our Board of Directors are granted restricted stock on the day of our annual meeting of stockholders and such shares of restricted stock vest on the date of the subsequent year's annual meeting of stockholders, provided such non-employee director remains a director on such date.

Restricted stock units ("RSUs") are granted to certain of our employees and generally vest over a period of four years and are expensed ratably on a straight-line basis over the vesting period. The fair value of both restricted stock and RSUs granted pursuant to our stock option plans is the product of the number of shares granted and the grant date fair value of our common stock. Our unrecognized compensation cost related to non-vested restricted stock at September 30, 2013 was approximately $0.6 million and is expected to be recognized over a weighted-average period of 0.6 years. Expected future compensation expense relating to RSUs outstanding on September 30, 2013 is $4.8 million over a weighted-average period of 2.2 years.

A summary of activity of both restricted stock and RSUs for the nine months ended September 30, 2013 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, 2012	58	$14.19	389	$14.09
Granted	55	$18.20	125	$18.12
Vested	(61)	$14.23	(98)	$13.90
Forfeited	—	$—	(21)	$14.07
Non-vested, September 30, 2013	52	$18.43	395	$15.41

Performance-Based Restricted Stock Units

In 2011, we began incorporating performance-based restricted stock units ("PSUs") as an element of our executive compensation plans. For 2011, we granted 100,000 PSUs; however, pursuant to their terms, 120,000 PSUs ultimately became eligible for vesting based on the achievement of a certain level of shareholder return for 2011 as described below. In 2012, we granted 125,000 PSUs of which 62,500 became eligible for vesting based on the achievement of a certain level of stockholder return for 2012 as described below.

Our unrecognized compensation cost related to non-vested performance-based restricted stock units at September 30, 2013 was approximately $1.5 million and is expected to be recognized over a weighted-average period of 1.3 years. For the three months ended September 30, 2013 and 2012, we recognized $0.4 million and $0.2 million, respectively, of compensation expense for the performance-based restricted stock units. For the nine months ended September 30, 2013 and 2012, we recognized $1.2 million and $0.8 million, respectively, of compensation expense for the performance-based restricted stock units.

The accounting guidance for awards with market conditions differs from that for awards with service conditions only or service and performance conditions. Because the grant date fair value of an award containing market conditions is calculated

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as the expected value, averaging over all possible outcomes, the measured expense is amortized over the service period, regardless of whether the market condition is ever actually met.

The fair value of a PSU award is the average of trial-specific values of the award over each of one million Monte Carlo trials. Each trial-specific value is the market value of the award at the end of the one-year performance period discounted back to the grant date. The market value of the award for each trial at the end of the performance period is the product of (a) the per share value of Omnicell stock at the end of the performance period and (b) the number of shares that vest. The number of shares that vest at the end of the performance period depends on the percentile ranking of the total stockholder return for Omnicell stock over the performance period relative to the total stockholder return of each of the other companies in the NASDAQ Healthcare Index (the "Index") as shown in the tables below.

Vesting for the PSU awards is based on the percentile placement of our total stockholder return among the companies listed in the Index and time-based vesting. We calculate total stockholder return based on the one year annualized rates of return reflecting price appreciation plus reinvestment of dividends. For PSU awards granted on February 5, 2013 and on March 5, 2013, stock price appreciation is calculated based on the average closing prices of our common stock for the last 20 trading days leading to February 28, 2014. For PSU awards granted in 2011 and 2012, stock price appreciation is calculated based on the average closing prices of the applicable company's common stock for the 20 trading days ending on the last trading day of the year prior to the date of grant as compared to the average closing prices for the 20 trading days ended on the last trading day of the year of grant.

The following table shows the percent of PSUs granted in 2011 and eligible for further time-based vesting based on our percentile placement:

Percentile Placement of Our Total Stockholder 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, but below the 65th percentile	100%
At least the 65th percentile, but below the 75th percentile (1)	110% to 119%
At or above the 75th percentile	120%

(1) The actual percentage of PSUs eligible for further time-based vesting is based on straight-line interpolation, where, for example, if the ranking is the 70th percentile, then the vesting percentage is 115%.

On January 17, 2012, the Compensation Committee of our Board of Directors confirmed 76.3% as the percentile rank of Omnicell’s 2011 total stockholder return. This resulted in 120% of the 2011 PSU awards, or 120,000 shares, becoming eligible for further time-based vesting. The eligible PSU awards will vest as follows: 25% of the eligible awards for the first year vested immediately on January 17, 2012 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. Of the 120,000 shares eligible for time-based vesting under the 2011 PSU awards, 10,000 shares vested during the year ended December 31, 2012.

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 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.

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On February 5 and March 5 2013, the Compensation Committee approved PSU awards of 125,000 shares and 12,500 shares, respectively. If the minimum performance threshold is met as determined by the Compensation Committee of the Board of Directors in 2014, 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 nine months ended September 30, 2013 is presented below:

Performance-based Stock Units	Number of Units (in thousands)	Weighted-Average Grant Date Fair Value Per Unit
Non-vested, December 31, 2012	175	$11.00
Granted	140	$14.74
Vested	(38)	$11.02
Forfeited	(24)	$—
Non-vested, September 30, 2013	253	$13.07

Employee Stock Purchase Plan

We have an Employee Stock Purchase Plan (“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. As of September 30, 2013, 4,233,557 shares had been issued under the ESPP. As of September 30, 2013 there were a total of 1,097,998 shares reserved for future issuance under the ESPP. For the three months and nine months ended September 30, 2013, 193,719 and 450,713 shares, respectively, of common stock were purchased under the ESPP.

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. 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, as described above.
The impact on our results for share-based compensation for the three and nine months ended September 30, 2013 and 2012 was as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Cost of product and service revenues	$325	$275	$955	$776
Research and development expenses	405	232	1,019	686
Selling, general and administrative expenses	2,080	1,854	6,449	5,319
Total share-based compensation expenses	$2,810	$2,361	$8,423	$6,781

Note 14. Business Acquisition

MTS Medication Technologies, Inc.

On May 21, 2012, we completed our acquisition of MedPak Holdings, Inc. ("MedPak") pursuant to an Agreement and Plan of Merger (the "Merger Agreement") under which Mercury Acquisition Corp, a newly formed Omnicell subsidiary, was merged with and into MedPak, with MedPak surviving the merger as a wholly-owned subsidiary of Omnicell. MedPak is the parent company of MTS Medication Technologies, Inc. ("MTS").

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The MTS acquisition primarily was to align Omnicell with the long term trends of the healthcare market to manage the health of patients across the continuum of care. We can now better 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.

We have accounted for the transaction under the acquisition method of accounting in accordance with the provisions of FASB ASC Topic 805, Business Combinations. Under the acquisition method, the estimated fair value of the consideration transferred to purchase the acquired company is allocated to the assets acquired and the liabilities assumed based on their fair values. We have made significant estimates and assumptions in determining the allocation of the acquisition consideration.

Pursuant to the terms of the Merger Agreement, we paid approximately $158.3 million in cash after adjustments provided for in the Merger Agreement, of which approximately $13.5 million was placed in an escrow fund, which will be distributed to MedPak's stockholders (subject to claims that we may make against the escrow fund for indemnification and other claims following the closing). The revised acquisition consideration of $158.3 million is comprised entirely of cash at closing.

At date of acquisition, we also recorded a $1.8 million liability based on expected additional working capital adjustments. In October 2012, a portion of the escrow fund set aside for the working capital adjustment was disbursed, with Omnicell receiving $0.3 million and MedPak's former stockholders receiving the remainder. As of December 31, 2012, the working capital adjustment was reversed, with a resulting reduction in goodwill of $1.8 million and a corresponding reduction in accrued liabilities. Accounts receivable acquired were recorded at their estimated fair value, comprised of total contractual obligations due of $7.6 million, of which $0.2 million was not expected to be collected. Based on an acquisition date valuation, the preliminary estimated fair values of acquired inventory and property and equipment exceeded their historical carrying values. We recorded a preliminary step-up to the estimated fair value of acquired inventory in the amount of $1.6 million, which resulted in subsequent related charges of $1.6 million to cost of product revenues.

In the fourth quarter of 2012, subsequent to the initial acquisition price allocation, we revised our preliminary determination of the fair value of fixed assets and intangible assets acquired from MTS, resulting in a decrease in the carrying value of acquired fixed assets of $1.3 million, and increase in the carrying value of intangibles of $0.4 million and a net increase in recorded goodwill of $0.9 million. During the first quarter of 2013, we reduced goodwill by $0.1 million due to an adjustment in stockholder's equity.

The total revised acquisition price was approximately $158.3 million and was allocated as follows (in thousands):

	Fair value acquired	
Cash including restricted cash	$2,000	
Accounts receivable	7,403	
Inventory	11,726	
Deferred tax assets and other current assets	2,894	
Total current assets	24,023	
Property and equipment	9,807	
Intangible assets	83,900	
Goodwill	82,800	
Other non-current assets	308	
Total assets	200,838	
Current liabilities	(7,917	)
Non-current deferred tax liabilities	(33,386	)
Other non-current liabilities	(1,223	)
Net assets acquired	$158,312	
Cash consideration, fair value	$158,312	

Identifiable intangible assets. Acquired technology relates to MTS' products across all of its product lines that have reached technological feasibility, primarily the OnDemand technology. Trade name is primarily related to the MTS and OnDemand brand names. Customer relationships represent existing contracted relationships with pharmacies, institutional care

facilities and others. Acquired technology, customer relationships, and trade names will be amortized on a straight-line basis over their estimated useful lives, which range from 12 to 30 years.
The estimated fair values of the acquired technology, trade names and customer relationships were primarily determined using either the relief-from-royalty or excess earnings methods. The interest rates utilized to discount net cash flows to their present values were determined after consideration of the overall enterprise rate of return and the relative risk and importance of the assets to the generation of future cash flows.
For income tax purposes, the historical tax bases of the acquired assets and assumed liabilities, along with the tax attributes of the MTS companies, will carry over. Because the transaction was a cash-for-stock transaction, there is no tax basis in the newly acquired intangible assets. Accordingly, the acquisition accounting includes the establishment of net deferred tax liabilities of $33.4 million, resulting from book tax basis differences related to the intangible assets acquired, as well as to the step up in the value of fixed assets and inventory to their estimated fair values at the time of acquisition.
Details of acquired intangibles are as follows (in thousands, except for years):

	Fair value acquired	Useful Life (years)	First year amortization expense
Trade name	$6,800	12	$ 567
Customer relationships	50,500	28 to 30	1,707
Acquired technology	26,600	20	1,330
Intangibles acquired	$83,900		$ 3,604
Weighted average life of intangibles		25.14	

Goodwill. Approximately $82.8 million has been allocated to goodwill. Goodwill represents the excess of the fair value of the consideration transferred over the fair value of the underlying net tangible and identifiable intangible assets on the acquisition date. In accordance with ASC Topic 350, Intangibles - Goodwill and Other, goodwill will not be amortized, but instead will be tested for impairment at least annually or more frequently if certain indicators are present. We believe the MTS acquisition enhances our offerings and diversifies our revenue mix, providing a more robust product and service solution to our current customers while expanding our international presence. We consider these factors as supporting the amount of goodwill recorded.
For the three and nine months ended September 30, 2013, we did not incur any acquisition-related costs in connection with the MTS acquisition. For the nine months ended September 30, 2012, we incurred approximately $3.2 million in acquisition related costs related to the MTS acquisition. These costs are included in selling, general and administrative expenses on our Condensed Consolidated Statement of Operations.

Note 15. Segments
Beginning with the acquisition of MTS 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 hospital settings.
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.

Since 1992, Omnicell has provided automation and business information solutions to 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 the acute care environment in hospitals. As the acute care market evolves, we see opportunities to provide medication adherence solutions, which were added to our

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product line through the acquisition of MTS. A portion of our organization structure and management processes will continue to be structured to optimize sales and service of solutions to the acute care market.
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. A portion of our organization structure and management processes will continue to be structured to optimize the product, sales, and service of solutions to the non-acute care market.
During 2012, we realigned our management reporting structure to report sales of Omnicell's dispensing systems and other related business transactions to long-term care pharmacies and facilities. Accordingly, the operations of this portion of our activities are now being reflected as a part of the Non-Acute Care segment for three and nine months ended September 30, 2013.
We believe that legislative changes and economic pressures to manage costs will cause healthcare organizations to manage the health of patients across the continuum of care regardless of the setting in which the care is provided. We believe we have the capabilities and market position to provide the tools needed by our customers to manage medications across the continuum of care. But we also believe that the inherent differences between medication management workflows in acute care settings and non-acute care settings will cause our product solutions and marketing strategies to be managed separately for these two customer segments.
Effective in the second quarter of 2013, our management changed its methodology for allocating certain expenses to our reportable segments. We have reclassified segment operating results for the three and nine months ended September 30, 2012 to conform to the 2013 presentation. For the three and nine months ended September 30, 2013 and 2012, the contributions of our segments to net revenues and income from operations, and the reconciliation to total net income, were as follows (amounts in thousands):

	Three Months Ended September 30, 2013			Three Months Ended September 30, 2012		
	Acute Care	Non-Acute Care	Total	Acute Care	Non-Acute Care (1)	Total
Net revenues from external customers	$70,640	$23,399	$94,039	$64,394	19,937	$84,331
Cost of revenues	28,662	13,337	41,999	26,920	11,324	38,244
Gross profit	$41,978	$10,062	$52,040	$37,474	$8,613	$46,087
Gross margin %	59.4 %	43.0 %	55.3 %	58.2 %	43.2 %	54.7 %
Operating expenses	32,908	8,415	41,323	29,070	5,791	34,861
Income from operations	$9,070	$1,647	$10,717	$8,404	2,822	$11,226
Operating margin %	12.8 %	7.0 %	11.4 %	13.1 %	14.2 %	13.3 %
Interest and other income (expense), net			25			34
Income before provision for income taxes			10,742			11,260
Provision for income taxes			2,987			4,340
Net income			$7,755			$6,920

(1) Non-Acute Care segment includes MTS results from May 21, 2012, the date of acquisition.

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	Nine Months Ended September 30, 2013			Nine Months Ended September 30, 2012		
	Acute Care	Non-Acute Care	Total	Acute Care	Non-Acute Care (1)	Total
Net revenues from external customers	$ 204,750	$ 70,085	$ 274,835	$ 191,295	$ 32,563	$ 223,858
Cost of revenues	87,784	40,276	128,060	82,859	19,787	102,646
Gross profit	$ 116,966	$ 29,809	$ 146,775	$ 108,436	$ 12,776	$ 121,212
Gross margin %	57.1 %	42.5 %	53.4 %	56.7 %	39.2 %	54.1 %
Operating expenses	96,048	26,483	122,531	94,167	9,753	103,920
Income from operations	$ 20,918	$ 3,326	$ 24,244	$ 14,269	3,023	$ 17,292
Operating margin %	10.2 %	4.7 %	8.8 %	7.5 %	9.3 %	7.7 %
Interest and other income (expense), net			(134)			57
Income before provision for income taxes			24,110			17,349
Provision for income taxes			6,954			6,703
Net income			$ 17,156			$ 10,646

(1) Non-Acute Care segment includes MTS results from May 21, 2012, the date of acquisition.

At September 30, 2013, segment assets were as follows (amounts in thousands):

	September 30, 2013			December 31, 2012		
	Acute Care	Non-Acute Care	Total	Acute Care	Non-Acute Care (1)	Total
Segment Assets	$ 284,067	$ 221,917	$ 505,984	$ 235,186	$ 206,633	$ 441,819

At three and nine months ended September 30, 2013 and 2012, segment depreciation/amortization, and capital expenditures were as follows (amounts in thousands):

	Three Months Ended September 30, 2013			Three Months Ended September 30, 2012		
	Acute Care	Non-Acute Care	Total	Acute Care	Non-Acute Care (1)	Total
Depreciation/Amortization	$ 2,805	$ 1,683	$ 4,488	$ 2,072	$ 1,842	$ 3,914
Capital Expenditures	1,311	745	2,056	$ 4,940	$ 532	$ 5,472

(1) Non-Acute Care segment includes MTS results from May 21, 2012, the date of acquisition.

	Nine Months Ended September 30, 2013			Nine Months Ended September 30, 2012		
	Acute Care	Non-Acute Care	Total	Acute Care	Non-Acute Care (1)	Total
Depreciation/Amortization	$ 8,351	$ 5,381	$ 13,732	$ 6,538	$ 2,709	9,247
Capital Expenditures	3,329	4,478	7,807	$ 8,947	$ 612	$ 9,559

(1) Non-Acute Care segment includes MTS results from May 21, 2012, the date of acquisition.

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Note 16. Asset Impairment

Impairment of Software Development Costs

As part of the continuing integration of MTS, during the first quarter of 2013, we reorganized our management team, including the software development department, within the Non-Acute Care segment. Through the end of the first quarter of 2013, the Non-Acute Care 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 $1.8 million ($0.03 per diluted share, net of tax), to expense as a component of research and development in the accompanying consolidated condensed statement of operations.

Note 17. Credit Agreement

In September 2013, we entered into a credit agreement (the "Credit Agreement") with Wells Fargo Bank, National Association, as administrative agent, and the lenders from time to time party thereto. The Credit Agreement provides for a $75.0 million revolving credit facility with a $10.0 million letter of credit sub-limit. Loans under the Credit Agreement mature on September 25, 2018. The Credit Agreement permits us to request one or more increases in the aggregate commitments provided that such increases do not exceed $25.0 million in the aggregate. We expect to use the proceeds from any revolving loans under the credit facility for general corporate purposes, including future acquisitions. Our obligations under the Credit Agreement are guaranteed by certain of our domestic subsidiaries and secured by substantially all of our and the subsidiary guarantors’ assets. To date, we have not yet drawn any funds under the credit facility.

Amounts drawn under the Credit Agreement bear interest, at our election, at a Eurodollar rate plus a margin of 1.75% per annum, or an alternate base rate equal to the highest of (a) the prime rate, (b) the federal funds rate plus 0.50%, and (c) LIBOR for an interest period of one month plus 1.75%. We are required to pay a commitment fee of 0.25% per annum on the aggregate undrawn amount of the commitments under the credit facility.

The Credit Agreement contains customary affirmative and negative covenants, including, among other things, restrictions on indebtedness, liens, investments, mergers, dispositions, dividends and other distributions. The Credit Agreement contains financial covenants that require us to, among other things, maintain a maximum consolidated total leverage ratio and a minimum consolidated fixed charge coverage ratio, in each case, as of the last day of each fiscal quarter. We were in full compliance with all covenants at September 30, 2013.

Item 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements. The forward looking statements are contained principally in the sections entitled “Risk Factors” and “Management's Discussion and Analysis of Financial Condition and Results of Operations.” These statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. Forward-looking statements include, but are not limited to, statements about:

- the extent and timing of future revenues, including the amounts of our current backlog, which represents firm orders that have not completed installation and therefore have not been recognized as revenue;
- the size or growth of our market or market share;
- the opportunity presented by new products or emerging markets;
- our expectations regarding our future backlog levels;
- our ability to align our cost structure and headcount with our current business expectations;
- the operating margins or earnings per share goals we may set;

- our ability to protect our intellectual property and operate our business without infringing upon the intellectual property rights of others;
- our ability to generate cash from operations and our estimates regarding the sufficiency of our cash resources; and
- our ability to acquire companies, businesses, products or technologies on commercially reasonable terms and integrate such acquisitions effectively.

In some cases, you can identify forward-looking statements by terms such as "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "will," "would" and similar expressions intended to identify forward-looking statements. Forward-looking statements reflect our current views with respect to future events, are based on assumptions and are subject to risks and uncertainties. We discuss many of these risks in this Quarterly Report on Form 10-Q in greater detail in Part II - Section 1A. “Risk Factors” below. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Also, forward-looking statements represent our estimates and assumptions only as of the date of this Quarterly Report on Form 10-Q. You should also read our Annual Report on Form 10-K and the documents that we reference in the Annual Report on Form 10-K and have filed as exhibits, completely and with the understanding that our actual future results may be materially different from what we expect. All references in this report to "Omnicell, Inc.," "Omnicell," "our," "us," "we," or the "Company" collectively refer to Omnicell, Inc., a Delaware corporation, and its subsidiaries. Except as required by law, we assume no obligation to update any forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in any forward-looking statements, even if new information becomes available in the future.

Overview

We are a leading provider of automation and business information solutions enabling healthcare systems to streamline the medication administration process and manage costly medical supplies for increased operational efficiency and enhanced patient safety. Our automation, analytics and medication adherence solutions are designed to enable healthcare facilities to acquire, manage, dispense and administer medications and medical-surgical supplies and are intended to enhance patient safety, reduce medication errors, reduce operating costs, improve workflow, and increase operational efficiency.

Approximately 2,800 hospitals use one or more of our products, of which more than 1,800 hospitals in the United States have installed our automated hardware/software solutions for controlling, dispensing, acquiring, verifying, tracking and analyzing medications and medical and surgical supplies. Approximately 6,000 institutional and retail pharmacies use our medication adherence packaging solutions.

The medical industry has become increasingly aware that human factors inevitably create the risk of medication administration errors in the course of patient care.

The Institute of Medicine, a non-profit, non-governmental arm of the National Academies, published a report in 2006 that estimated that 1.5 million medication errors are made each year in the United States. Acute care facilities are required to adhere to medication regulatory controls that we believe cannot be adequately supported by manual tracking systems or partially automated systems. Nursing shortages add an additional challenge to acute care facilities to meet regulatory controls and improve patient safety while still providing adequate patient care. Non-acute care facilities face similar safety challenges. According to "Adherence to Long-Term Therapies-Evidence for Action," the World Health Organization has stated, “Across diseases, adherence is the single most important modifiable factor that compromises treatment outcome.” U.S. health system thought leaders see medication adherence as a key requirement for closing the medication loop and delivering better clinical outcomes and financial results. Medication non-adherence is described as a critical problem creating approximately $290 billion in extra costs, according to the New England Healthcare Institute, resulting in approximately 125,000 deaths per year. In addition, the Centers for Medicare & Medicaid Services states that 11% of all hospital admissions are related to medication non-adherence.

We provide solutions to help healthcare systems and caregivers address these problems. We believe that our patient-centric medication and supply management solutions help improve workflow efficiencies and patient outcomes.

Business Segments

Our business is organized 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.

Acute Care

In acute care facilities, our solutions use advanced, software based medication control and tracking algorithms that interact with hardware security features, resulting in a system that provides both the pharmacist and the nurse real-time safety controls. Our solutions also go a step further by providing medication bar code verification at every step of the medication administration process, from entry to the hospital through to administration to a patient. Our systems enable our customers to reduce or eliminate inefficiencies such as manual tracking and reconciliations, nursing time spent in obtaining medications and in performing inventory control and extraneous process steps.

Similar to our medication solutions, our medical and surgical supply systems provide acute care hospitals control over consumable supplies critical to providing quality healthcare. Our solutions provide inventory control software that is designed to ensure critical supplies are always stocked in the right locations. At the same time, usage tracking helps hospital administrators to ensure that money is not wasted on excessive stores of supplies and helps optimize reimbursement by improving charge capture. Our systems automate the tracking of activities in perioperative areas such as the operating room and catheter lab, including tracking implantable tissue grafts for additional patient safety and regulatory compliance.

Additionally, we offer analytics and reporting software for pharmacists and material managers to more easily manage inventory flow, tracking and optimization. These reports are often used to identify hospital employees who may be improperly diverting pharmaceuticals stored in the automated dispensing cabinets. Such diversion or theft, especially of controlled substances, could result in black market sales or other illicit uses.

Non-Acute Care

Our Non-Acute Care product lines were primarily added to our solutions through the acquisition of MTS Medication Technologies, Inc. ("MTS"), a worldwide provider of medication adherence packaging systems, and a wholly-owned Omnicell subsidiary. MTS manufactures proprietary medication dispensing systems and related products for use by institutional pharmacies servicing long-term care and correctional facilities and retail pharmacies servicing patients caring for themselves at home. These systems use consumable medication punch cards and specialized machines that allow the pharmacies to automatically or semi-automatically assemble, fill and seal drugs into medication punch cards representing a weekly or monthly supply of a patient's medication. The use of these cards and machines provides a cost-effective customized package personalized to the patient. The punch card medication dispensing system provides tamper evident packaging and promotes medication compliance.

Our Non-Acute Care systems are used by institutional pharmacists to package medications into blister cards that form the backbone of medication control in non-acute care facilities. Our line of equipment provides solutions ranging from low cost semi-automated packaging systems to fully automated robotic systems that help eliminate human error and increase the efficiency of packaging medication for non-acute care facilities. Our OnDemand line of multi-medication packaging equipment can be used by retail pharmacies to provide enhanced packages that we believe increase the probability that patients will adhere to the medication regimen prescribed by their healthcare provider.

Our Non-Acute Care segment manufactures and sells consumable medication blister cards, packaging equipment and ancillary products, as well as automated dispensing equipment used in long term care facilities throughout the United States, Canada, Europe and Australia. This segment's customers are predominantly institutional and independent retail pharmacies that supply nursing homes, assisted living and correctional facilities with prescription medications for their patients. We manufacture our proprietary consumable blister cards and most of our packaging equipment in our own facilities. This manufacturing process uses integrated equipment for manufacturing the consumable medication blister cards. In addition, we utilize the services of contract manufacturers for some of our packaging equipment. We distribute products directly in the United Kingdom and in Germany through our subsidiaries in those countries.

Our solutions are aligned with the long-term trends of the healthcare market to assist in the management of patient health across the continuum of care.

Our key business strategies include:

- Further penetrating the existing market through providing differentiated, innovative solutions, which includes:
- Consistently innovating our product and service offerings; and

- Maintaining our flexibility in customer product design and in the installation process to provide solutions tailored to our customers.
- Increasing penetration of new markets by:

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- Bringing new products and technologies to market that are specific to international markets;
- Bringing new products and technologies to market that address currently unsolved problems;
- Establishing direct sales, distribution or other capabilities when and where it is appropriate;
- Partnering with companies that have sales, distribution or other capabilities that we do not possess; and
- Increasing customer awareness of safety issues in the administration of medications.
- Expanding our product offering through acquisitions and partnerships.

Operations During the Three and Nine Months Ended September 30, 2013

The consolidated operating results presented for the nine months ended September 30, 2013 and the nine months ended September 30, 2012, reflect the impact of the acquisition of MTS since May 21, 2012 as a part of the Non-Acute Care segment.

Revenues grew year-over-year for both product and services, with overall revenue growth of 11.5%, comparing $94.0 million for the third quarter of 2013 with $84.3 million for the third quarter of 2012. Overall revenue growth was 22.8% for the nine months ended September 30, 2013 comparing $274.8 million with $223.9 million for the same period in 2012. Much of the growth was a result of the acquisition of MTS, which now comprises a substantial portion of the Non-Acute Care segment, and whose prior year operating results were not included in our consolidated operating results prior to the date of acquisition.

For the three months ended September 30, 2013, the Non-Acute Care segment contributed $22.2 million and $1.2 million to the product and service revenue, respectively as compared to $18.7 million and $1.2 million during the same period in 2012. The Acute Care segment contributed revenues of $53.3 million and $17.3 million to product and service revenue respectively, for the three months ended September 30, 2013 as compared to $48.8 million and $15.6 million during the same period in 2012. Overall product and service gross margins increased by $6.0 million, or 12.9% for the three months ended September 30, 2013 as compared to the same period in 2012.

For the nine months ended September 30, 2013, the Non-Acute Care segment contributed $66.4 million and $3.7 million, respectively, to the overall product and service revenue as compared to $30.2 million and $2.3 million during the same period in 2012. The Acute Care segment contributed revenues of $153.9 million and $50.8 million to product and service revenue, respectively, for the nine months ended September 30, 2013 as compared to $145.0 million and $46.3 million during the same period in 2012. Overall product and service gross margins increased by $25.6 million, or 21.1% for the nine months ended September 30, 2013 as compared to the same period in 2012.

During the three months ended September 30, 2013, total revenue remained relatively flat at $94.0 million as compared with $93.7 million for the three months ended June 30, 2013 with service revenues accounting for the majority of this increase. Overall gross margins for the third quarter of 2013 increased to 55.3% from 52.7% in the three months ended June 30, 2013. Product gross margins increased to 55.0% on revenue of $75.5 million for the three months ended September 30, 2013 as compared with 52.0% on revenue of $75.6 million during the second quarter of 2013. Service gross margins also increased, to 56.7% on revenue of $18.5 million as compared to 55.6% on $18.1 million in revenue during the second quarter of 2013.

Cash, cash equivalents and short-term investments increased by $53.9 million during the nine months ended September 30, 2013, to $116.2 million from $62.3 million at December 31, 2012 primarily due to increased profitability, working capital improvements and cash received for shares issued under our stock option and employee stock purchase plans.

During the nine months ended September 30, 2013, we implemented a reorganization within our Non-Acute Care segment. This reorganization reduced headcount slightly and as a result, we incurred $0.7 million in severance and related expenses and an additional $0.4 million related to accelerated stock option vesting in the first quarter of 2013.

This reorganization is intended to promote a stronger integration strategy, customer and segment focus, and future growth. As our business evolves, we will continue to assess our segments which could result in future modifications to the current presentation.

Critical Accounting Policies and Estimates

Management's discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of any contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We regularly review our estimates and assumptions, which are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of certain assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates and assumptions. We believe that the following critical accounting policies are affected by significant judgments and estimates used in the preparation of our condensed consolidated financial statements:

•Revenue recognition;
•Provision for allowances;
•Valuation and impairment of goodwill, other intangible assets and other long lived assets;
•Inventory;
•Valuation of share-based awards; and
•Accounting for income taxes.

During the nine months ended September 30, 2013, there were no significant changes in our critical accounting policies and estimates.

Please refer to Management’s Discussion and Analysis of Financial Condition and Results of Operations contained in Part II, Item 7 of our Annual Report on Form 10-K for our fiscal year ended December 31, 2012 for a more complete discussion of our other critical accounting policies and estimates.

Recently Adopted Accounting Standards

In February 2013, 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.

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Results of Operations

The table below shows the components of our consolidated results of operations as percentages of total revenues for the three months and nine months ended September 30, 2013 and 2012 (in thousands, except percentages):

	Three Months Ended September 30,					
	2013			2012		
	$	% of Revenue		$	% of Revenue	
Revenues:						
Product revenue	$75,508	80.3	%	$67,446	80.0	%
Service and other revenues	18,531	19.7	%	16,885	20.0	%
Total revenues	94,039	100.0	%	84,331	100.0	%
Cost of revenues:						
Cost of product revenues	33,977	36.1	%	30,636	36.3	%
Cost of service and other revenues	8,022	8.5	%	7,608	9.0	%
Total cost of revenues	41,999	44.6	%	38,244	45.3	%
Gross profit	52,040	55.4	%	46,087	54.7	%
Operating expenses:						
Research and development	6,561	7.0	%	5,545	6.6	%
Selling, general and administrative	34,762	37.0	%	29,316	34.8	%
Total operating expenses	41,323	44.0	%	34,861	41.4	%
Income from operations	10,717	11.4	%	11,226	13.3	%
Interest and other income (expense), net	25	—	%	34	—	%
Income before provision for income taxes	10,742	11.4	%	11,260	13.3	%
Provision for income taxes	2,987	3.2	%	4,340	5.1	%
Net income	$7,755	8.2	%	$6,920	8.2	%

	Nine Months Ended September 30,			
	2013		2012	
	$	% of Revenue	$	% of Revenue
Revenues:				
Product revenue	$220,325	80.2 %	$175,239	78.3 %
Service and other revenues	54,510	19.8 %	48,619	21.7 %
Total revenues	274,835	100.0 %	223,858	100.0 %
Cost of revenues:				
Cost of product revenues	103,810	37.8 %	79,532	35.5 %
Cost of service and other revenues	24,250	8.8 %	23,114	10.3 %
Total cost of revenues	128,060	46.6 %	102,646	45.8 %
Gross profit	146,775	53.4 %	121,212	54.2 %
Operating expenses:				
Research and development	21,665	7.9 %	17,538	7.8 %
Selling, general and administrative	100,866	36.7 %	86,382	38.6 %
Total operating expenses	122,531	44.6 %	103,920	46.4 %
Income from operations	24,244	8.9 %	17,292	7.8 %
Interest and other income (expense), net	(134)	— %	57	— %
Income before provision for income taxes	24,110	8.9 %	17,349	7.8 %
Provision for income taxes	6,954	2.5 %	6,703	3.0 %
Net income	$17,156	6.4 %	$10,646	4.8 %

The consolidated results presented above include the operating results of MTS since May 21, 2012, the date of acquisition and are included as part of the Non-Acute Care segment.

Effective in the second quarter of 2013, our management changed its methodology for allocating certain expenses to its reportable segments. We have reclassified segment operating results for the three and nine months ended September 30, 2012 to conform to the 2013 presentation.

Product Revenues, Cost of Product Revenues and Gross Profit

The table below shows our consolidated product revenues, cost of product revenues and gross profit for the three months and nine months ended September 30, 2013 and 2012 and the percentage changes between those periods (in thousands, except percentages):

	Three Months Ended September 30,		
	2013	2012	% Change
Product revenues	$75,508	$67,446	12.0 %
Cost of product revenues	33,977	30,636	10.9 %
Gross profit	$41,531	$36,810	12.8 %
Gross margin	55.0 %	54.6 %	0.4 %

	Nine Months Ended September 30,		
	2013	2012	% Change
Product revenues	$220,325	$175,239	25.7 %
Cost of product revenues	103,810	79,532	30.5 %
Gross profit	$116,515	$95,707	21.7 %
Gross margin	52.9 %	54.6 %	(1.7)%

Product revenues increased by $8.1 million, or 12.0%, in the three months ended September 30, 2013 as compared to the same period in 2012. Product revenues increased by $45.1 million, or 25.7%, in the nine months ended September 30, 2013 as compared to the same period in 2012.

The overall increase in product revenues for the three months ended September 30, 2013 was primarily driven by increased installations of our automation products in both the Non-Acute Care and Acute Care segments. The Non-Acute Care segment contributed $22.2 million as compared with $18.7 million for the same period last year. Our Acute Care segment contributed $53.3 million in product revenue for the three months ended September 30, 2013 as compared to $48.8 million for the same period in 2012.

The overall increase in product revenues for the nine months ended September 30, 2013 was primarily driven by a full nine month contribution of MTS activities as a part of our Non-Acute Care segment, which contributed $66.4 million during the period. This compared to $30.2 million in the same nine month period in 2012. Our Acute Care segment contributed $153.9 million in product revenue for the nine months ended September 30, 2013 compared to $145.0 million in the same nine month period in 2012.

We anticipate our revenues will continue to increase in 2013 compared to the same periods in 2012, as we fulfill our existing orders. Additionally, year over year revenue growth for the remainder of 2013 will continue to benefit from the contribution of our Non-Acute Care segment, including those of MTS, which we began to consolidate on May 21, 2012. Our ability to continue to grow revenue is dependent on our ability to continue to obtain orders from customers, our ability to produce quality consumables to fulfill customer demand, the volume of installations we are able to complete and our ability to meet customer needs by providing a quality installation experience and our flexibility in manpower allocations among customers to complete installations on a timely basis. The timing of our product revenues for equipment is primarily dependent on when our customers' schedules allow for installations.

Cost of product revenues increased by $3.3 million, or 10.9%, in the three months ended September 30, 2013 as compared to the same period in 2012. Cost of product revenues increased by $24.3 million, or 30.5%, in the nine months ended September 30, 2013 as compared to the same period in 2012.

The Non-Acute Care segment contributed product costs of $12.8 million for the three months ended September 30, 2013. Our Acute Care product cost increased by $1.4 million to $21.2 million, which is primarily a function of changes in revenue and product mix.

The increase in cost of product revenues for the nine months ended September 30, 2013 was primarily a result of a full nine months of Non-Acute Care product costs of $38.6 million. Our Acute Care product cost increased by $4.8 million to $65.2 million for the nine months ended September 30, 2013 as a result of changes in revenue and product mix.

Gross profit on product revenue increased by $4.7 million, or 12.8%, in the three months ended September 30, 2013 as compared to the same period in 2012. Gross profit on product revenue increased by $20.8 million, or 21.7%, in the nine months ended September 30, 2013 as compared to the same period in 2012. Our Non-Acute Care segment gross profit on product revenue increased $1.6 million and $16.7 million for the three months and nine months ended September 30, 2013, respectively. Our Acute Care gross profit on product revenue increased by $3.2 million and $4.1 million for the three months and nine months ended September 30, 2013, respectively, as compared to the same period in 2012 primarily due to changes in product mix.

Service and Other Revenues, Cost of Service and Other Revenues and Gross Profit

The table below shows our service and other revenues, cost of service and other revenues and gross profit for the three months and nine months ended September 30, 2013 and 2012 and the percentage change between those periods (in thousands, except percentages):

	Three Months Ended September 30,		
	2013	2012	% Change
Service and other revenues	$18,531	$16,885	9.7 %
Cost of service and other revenues	8,022	7,608	5.4 %
Gross profit	$10,509	$9,277	13.3 %
Gross margin	56.7 %	54.9 %	1.8 %

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	Nine Months Ended September 30,		
	2013	2012	% Change
Service and other revenues	$54,510	$48,619	12.1 %
Cost of service and other revenues	24,250	23,114	4.9 %
Gross profit	$30,260	$25,505	18.6 %
Gross margin	55.5 %	52.5 %	3.0 %

Service and other revenues include revenues from service and maintenance contracts, rentals of automation systems, and training and professional services. Service and other revenues increased by $1.6 million, or 9.7%, in the three months ended September 30, 2013 as compared to the same period in 2012. Service and other revenues increased by $5.9 million, or 12.1%, in the nine months ended September 30, 2013 as compared to the same period in 2012. These increases in service and other revenues were primarily the result of our installation of automation systems during the year which increases the installed base, adding more automation systems under service contracts.

Our Non-Acute Care segment contributed services and other revenues of $1.2 million for the three months ended September 30, 2013 consistent with the same period in 2012. Our Acute Care segment contributed $17.3 million in services and other revenues for the three months ended September 30, 2013 as compared to $15.6 million for the same period in 2012.

Our Non-Acute Care segment contributed services and other revenues of $3.7 million for the nine months ended September 30, 2013 compared to $2.3 million for the same period in 2012 driven by services for MTS branded products after the acquisition of MTS in 2012. Our Acute Care segment contributed $50.8 million in service and other revenues for the nine months ended September 30, 2013 and $46.3 million for the same period in 2012.

Cost of service and other revenues increased by $0.4 million, or 5.4%, in the three months ended September 30, 2013 as compared to the same period in 2012. The increase in cost of service and other revenues was primarily the result of an increase in the costs associated with increased service revenues as a result of expansion in our Acute Care segment installed base of automation systems. Cost of service and other revenues increased by $1.1 million, or 4.9%, in the nine months ended September 30, 2013 as compared to the same period in 2012, primarily driven by a full nine months of costs attributable to our Non-Acute Care segment of $1.7 million. Our Acute Care cost of service and other revenues was relatively flat as compared with the same period a year ago as a result of cost reduction efforts that resulted in revenues growing at a faster rate than costs.

Gross profit on service and other revenues increased by $1.2 million, or 13.3%, in the three months ended September 30, 2013 as compared to the same period in 2012. Gross profit on service and other revenues increased by $4.8 million, or 18.6%, in the nine months ended September 30, 2013 as compared to the same period in 2012. The increase in gross profit on service and other revenues was primarily due to increased revenues from an expanded installed base with only a slight increase in associated service costs. Gross profit on service and other revenues from our Non-Acute Care segment was $0.6 million and from our Acute Care segment was $9.9 million in the three months ended September 30, 2013. Our Acute Care gross profit on service and other revenues increased by $1.3 million and $4.5 million for the three months and nine months ended September 30, 2013, respectively as compared to the same period in 2012.
We expect our service and other revenues and the associated gross profit to continue to increase in 2013 with the continued expansion of our installed base of automation systems and service and maintenance contracts and the addition of our Non-Acute Care segment.
Operating Expenses

The table below shows our operating expenses for the three and nine months ended September 30, 2013 and 2012 and the percentage changes between those periods (in thousands, except percentages):

	Three Months Ended September 30,			
	2013	2012	% Change	
Research and development	$6,561	$5,545	18.3	%
Selling, general and administrative	34,762	29,316	18.5	%
Total operating expenses	$41,323	$34,861	18.5	%

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	Nine Months Ended September 30,			
	2013	2012	% Change	
Research and development	21,665	17,538	23.5	%
Selling, general and administrative	100,866	86,382	16.8	%
Total operating expenses	$ 122,531	$ 103,920	17.9	%

Research and Development. Research and development expenses increased by $1.0 million, or 18.3%, in the three months ended September 30, 2013 as compared to the same period in 2012 and represented 7.0% and 6.6% of total revenues in the three months ended September 30, 2013 and 2012, respectively. The overall increase in research and development expenses is primarily due to a $0.8 million increase in research and development expenses attributable to the Non-Acute Care segment including $0.3 million related to medication cabinets, $0.2 million increase in consulting related expense and $0.3 million decrease in capitalization software effort.

Research and development expenses increased by $4.1 million, or 23.5%, in the nine months ended September 30, 2013 as compared to the same period in 2012 and represented 7.9% and 7.8% of total revenues in the nine months ended September 30, 2013 and 2012, respectively. The overall increase in research and development expenses reflects a $5.0 million increase in research and development expenses attributable to the Non-Acute Care segment, which includes a $1.8 million write-off of previously capitalized software development costs, discussed further in Note 16, "Asset Impairment" a $0.3 million charge related to the previously mentioned reorganization, and the inclusion of MTS headcount, consulting and other related activities for a full nine months in the 2013 period as compared with the prior period, which included MTS activities only since the date of the MTS acquisition in May 2012. These increases were offset by a $0.9 million decrease in the Acute Care segment which was comprised primarily of an increase of capitalized software costs of $2.7 million in connection with a higher level of post-feasibility beta testing and $0.6 million decrease in consulting related expense, offset by approximately $2.5 million increases in headcount related expenses.

We expect research and development expenses to remain relatively flat as a percentage of our revenue on an annual basis and to grow in absolute dollars in the future as our revenue grows to improve and enhance our existing technologies and to create new technologies in health care automation.

Selling, General and Administrative. Selling, general and administrative expenses increased by $5.4 million, or 18.5%, in the three months ended September 30, 2013 as compared to the same period in 2012. Selling, general and administrative expenses represented 37.0% and 34.8% of total revenues in the three months ended September 30, 2013 and 2012, respectively. The overall increase in selling, general and administrative expenses reflects a $1.9 million increase in selling, general and administrative expenses attributable to the Non-Acute Care segment. The Acute Care segment increase of $3.6 million was primarily due to $1.3 million in commission expenses associated with increased revenue, $0.6 million in facility and depreciation expenses for our new headquarters and manufacturing buildings occupied late in 2012, $0.5 million in professional fees, $0.6 million employee related expenses and $0.6 million in other compensation expenses related to long term incentive bonuses.

Selling, general and administrative expenses increased by $14.5 million, or 16.8% in the nine months ended September 30, 2013 as compared to the same period in 2012. Selling, general and administrative expenses represented 36.7% and 38.6% of total revenues in the nine months ended September 30, 2013 and 2012, respectively. The increase was primarily due to an increase in the Non-Acute Care selling, general and administrative expenses of $11.7 million representing the overall expenses incurred due to the inclusion of MTS activities for a full nine months in the 2013 period as compared with the prior period, which included MTS activities only since the date of the MTS acquisition in May 2012, included in this increase is $3.0 million of corporate allocation related to the Non-Acute cabinet segment. The Acute Care segment increase of $2.8 million was primarily due to $2.9 million in facility and depreciation expenses for our new headquarters and manufacturing buildings occupied late in 2012, $2.4 million in headcount-related expenses, $1.4 million increase in consulting and professional fees, $0.6 million in travel, entertainment, promotional and tradeshow related expenses, $0.5 million in GPO fees associated with higher collections and sales volume for GPO-affiliated customers, partially offset by $2.3 million of MTS acquisition related costs incurred in the 2012 period and a decrease of $2.8 million in allocations and miscellaneous general expenses of which the primary decrease was due to higher corporate allocation to the Non-Acute segment noted above.

We expect selling, general and administrative expenses to grow at a nominal rate in order to support our anticipated growth as well as international expansion efforts, but anticipate that increased efficiencies will result in a lower selling, general and administrative expense relative to total revenue growth in the future.

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Share-based Compensation. The effect of share-based compensation on functional expenses within our operating results for the three months and nine months ended September 30, 2013 and 2012 is presented in Note 13, "Stock Option Plans and Share-Based Compensation."

Provision for Income Taxes

The annual effective tax rate before discrete items was 38.1% and 41.5% for the nine months ended September 30, 2013 and 2012, respectively. The decrease in the estimated annual effective tax rate for the nine months ended September 30, 2013 as compared to the same period in 2012 was primarily due to the reinstatement of the federal research and development credit in January of 2013 along with a decrease in other non-deductible expenditures. The impact of these amounts was 2.2% and1.2%, respectively.

Liquidity and Capital Resources

We had cash and cash equivalents of $116.2 million at September 30, 2013, as compared to $62.3 million at December 31, 2012. All of our cash is invested in short term money market funds or demand deposits. We did not hold any short or long term investments as of September 30, 2013.

In September 2013, we entered into a Credit Agreement with Wells Fargo Bank, National Association, as administrative agent, and the lenders from time to time which provides for a $75.0 million revolving credit facility to be used for general corporate purposes, including future acquisitions. The Credit Agreement permits us to request one or more increases in the aggregate commitment provided such increases do not exceed $25.0 million in the aggregate. Please review details discussed in Note 17, "Credit Agreement."

We believe our current cash and cash equivalent balances and cash flows generated by operations, along with the availability of funds under our $75.0 million Credit Agreement, will be sufficient to satisfy our anticipated cash needs for working capital and capital expenditures for at least the next twelve months.

Cash flows for the nine months ended September 30, 2013 and 2012 consisted of the following (in thousands):

	Nine Months Ended September 30,	
	2013	2012
Net cash provided by operating activities	$40,737	$27,477
Net cash used in investing activities	(13,736)	(161,171)
Net cash provided by (used in) financing activities	26,847	(3,250)
Effect of exchange rate changes on cash and cash equivalents	29	—
Net increase in cash and cash equivalents	$53,877	$(136,944)

Operating activities provided $40.7 million of cash during the nine months ended September 30, 2013 as compared to $27.5 million for the same period in 2012. The main drivers of this increase were a $6.5 million increase in net income, a $4.3 million increase in accounts payable due to timing of payments, a $3.8 million increase in accrued liabilities, and a $2.8 million decrease in net investments in sales-types leases. These amounts were partially offset by a $7.6 million increase in inventory due to increased production to meet future demands, a $2.5 million decrease in deferred service revenue, and a $1.9 million increase in accounts receivable due to increased sales. Also impacting operating cash flows are non-cash adjustments which include a $4.5 million increase in depreciation and amortization, a $1.8 million asset impairment charge related to a software development project and a $1.6 million increase in share-based compensation expense.

Cash used in investing activities totaled $13.7 million during the nine months ended September 30, 2013, as compared to $161.2 million cash used in investing activities during the same period in 2012. This $147.4 million decrease in cash used primarily reflects a decrease of $156.3 million of net cash used to acquire MTS in May of 2012 and a decrease of $1.7 million for purchases of property and equipment. This was offset in part by a decrease of $8.1 million in proceeds from short-term investments and an increase of $2.6 million of capitalized software development costs during the nine months ended September 30, 2013.

Cash provided by financing activities was $26.8 million during the nine months ended September 30, 2013, as compared to $3.3 million used during the same period in 2012. The increase of $30.1 million is primarily due to an increase of $17.2 million in cash generated from shares issued under stock option and employee stock purchase plans during the nine months ended September 30, 2013 as compared to the same period in 2012 combined with no stock repurchase activity during

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the nine months ended September 30, 2013 as compared to the $12.4 million of cash used in stock repurchase activities during the nine months ended September 30, 2012.

Contractual Obligations

There have been no material changes to our contractual obligations during the nine months ended September 30, 2013. Please refer to our Annual Report on Form 10-K for the year ended December 31, 2012 for a description of our facility leases and contractual obligations and the Notes to the consolidated financial statements included therein.

The following table summarizes our contractual obligations at September 30, 2013 (in thousands):

	Total	Less than one year	One to three years	Three to five years	More than five years
Operating leases (1) (2)	$43,176	$ 5,772	$10,727	$8,980	$17,697
Commitments to contract manufacturers and suppliers (3)	7,520	7,520			
Total (4)	$50,696	$ 13,292	$10,727	$8,980	$17,697

(1) Commitments under operating leases relate primarily to leasehold property and office equipment.

(2) In October 2011, we entered into a lease agreement for approximately 100,000 square feet of office space. Pursuant to the lease agreement, the landlord constructed a single, three-story building of rentable space in Mountain View, California which we lease and which serves as our headquarters. The term of the lease agreement, which commenced in November 2012, is for a period of 10 years, with a base lease commitment of approximately $40.0 million. We have two options to extend the term of the lease agreement at market rates. Each extension is for an additional 60 month term.

(3) 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.

(4) At September 30, 2013, we have recorded $4.7 million for uncertain tax positions under long term liabilities, in accordance with GAAP, summarized under Note 1, “Organization and Summary of Significant Accounting Policies.” As these liabilities do not reflect actual tax assessments, the timing and amount of payments we might be required to make will depend upon a number of factors. Accordingly, as the timing and amount of payment cannot be estimated, the current balance of the uncertain tax position liabilities has not been included in the table of commitments above.

Off-Balance Sheet Arrangements

As of September 30, 2013, we had no off-balance sheet arrangements as defined in Regulation S-K 303(a)(4)(ii) of the Securities Exchange Act of 1934, as amended, and the instructions thereto.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of September 30, 2013, there were no material changes to our disclosures to market risk from the disclosures set forth under the caption, “Quantitative and Qualitative Disclosures About Market Risk” in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2012.

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of September 30, 2013. Based on such evaluation, our principal executive officer and principal financial officer have concluded that, as of September 30, 2013, our disclosure controls and procedures were effective.

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Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the three months ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

Legal Proceedings

The information set forth under “Legal Proceedings” in Note 11, “Contingencies,” of the Notes to Consolidated Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q for the period ended September 30, 2013 is incorporated herein by reference.

Item 1A. RISK FACTORS

We have identified the following risks and uncertainties that may have a material adverse effect on our business, financial condition or results of operations. Our business faces significant risks and the risks described below may not be the only risks we face. Additional risks not presently known to us or that we currently believe are immaterial may also significantly impair our business operations. If any of these risks occur, our business, results of operations or financial condition could suffer and the market price of our common stock could decline.

Unfavorable economic and market conditions, a decreased demand in the capital equipment market and uncertainty regarding the rollout of government legislation in the healthcare industry could adversely affect our operating results.

Customer demand for our products is significantly linked to the strength of the economy. If decreases in demand for capital equipment caused by weak economic conditions and decreased corporate and government spending, including any effects of fiscal budget balancing at the federal level effective in 2013, deferrals or delays of capital equipment projects, longer time frames for capital equipment purchasing decisions or generally reduced expenditures for capital solutions continues, we will experience decreased revenues and lower revenue growth rates and our operating results could be materially and adversely affected.

Additionally, as the U.S. Federal government implements healthcare reform legislation, and as Congress, regulatory agencies and other state governing organizations continue to review and assess additional healthcare legislation and regulations, there may be an impact on our business. Healthcare facilities may decide to postpone or reduce spending until the implications of such healthcare enactments are more clearly understood, which may affect the demand for our products and harm our business.

The medication management and supply chain solutions market is highly competitive and we may be unable to compete successfully against new entrants and established companies with greater resources and/or existing business relationships with our current and potential customers.

The medication management and supply chain solutions market is intensely competitive. We expect continued and increased competition from current and future competitors, many of which have significantly greater financial, technical, marketing and other resources than we do. Our current direct competitors in the medication management and supply chain solutions market include CareFusion Corporation (which includes Pyxis Corporation, PhACTs LLC and Rowa Technologies), Aesynt (through Francisco Partners' acquisition of McKesson Automation Inc.), AmerisourceBergen Corporation (through its acquisition of MedSelect, Inc. and Automed), Cerner Corporation, Talyst, Inc., Emerson Electronic Co. (through its acquisitions of Flo Healthcare LLC, Lionville Systems, Inc. and medDispense, L.P.), Swisslog Holding AG, Stinger Medical, Stanley Black and Decker, Inc. (through their acquisition of InfoLogix, Inc.), Ergotron, Inc., Capso Solutions LLC (through their acquisition of Artromick International, Inc.), Rubbermaid Medical Solutions (a business unit of Newell Rubbermaid Inc.), WaveMark Inc., ParExcellence Systems, Inc., Vanas n.v., Lawson Software, Inc. and MACH4 Automatisierungstechnik GmbH. Our current direct competitors in the medication packaging solutions market include Drug Package, Inc., AutoMed® Technologies, Inc. (a subsidiary of AmerisourceBergen Corporation), Manchac Technologies, LLC (through its Dosis product line) and RX Systems, Inc. in the United States, and Surgichem Ltd., and Jones Packaging Ltd. in Europe.

The competitive challenges we face in the medication management and supply chain solutions market include, but are not limited to, the following:

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certain competitors may develop new features or capabilities for their products not previously offered that could compete directly with our products;

- competitive pressures could result in increased price competition for our products and services, fewer customer orders and reduced gross margins, any of which could harm our business;
- current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with third parties, including larger, more established healthcare supply companies, thereby

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increasing their ability to develop and offer products and services to address the needs of our prospective customers;

- our competitors may develop, license or incorporate new or emerging technologies or devote greater resources to the development, promotion and sale of their products and services than we do;
- certain competitors have greater brand name recognition and a more extensive installed base of medication and supply dispensing systems or other products and services than we do, and such advantages could be used to increase their market share;
- certain competitors may have existing business relationships with our current and potential customers, which may cause these customers to purchase medication and supply dispensing systems or automation solutions from these competitors;
- other established or emerging companies may enter the medication management and supply chain solutions market; and
- our competitors may secure products and services from suppliers on more favorable terms or secure exclusive arrangements with suppliers or buyers that may impede the sales of our products and services.

Any reduction in the demand for or adoption of our medication and supply systems, related services, or consumables would reduce our revenues.

Our medication and supply dispensing systems represent only one approach to managing the distribution of pharmaceuticals and supplies at acute healthcare facilities and our medication packaging systems represent only one way of managing medication distribution at non-acute care facilities. A significant portion of domestic and international healthcare facilities still use traditional approaches in some form that do not include fully automated methods of medication and supply management. As a result, we must continuously educate existing and prospective customers about the advantages of our products, which requires significant sales efforts and can cause longer sales cycles. Despite our significant efforts and extensive time commitments in sales to healthcare facilities, we cannot be assured that our efforts will result in sales to these customers.

In addition, our medication and supply dispensing systems and our more complex automated packaging systems typically represent a sizable initial capital expenditure for healthcare organizations. Changes in the budgets of these organizations and the timing of spending under these budgets can have a significant effect on the demand for our medication and supply dispensing systems and related services. These budgets are often supported by cash flows that can be negatively affected by declining investment income and influenced by limited resources, increased operational and financing costs, macroeconomic conditions such as unemployment rates and conflicting spending priorities among different departments. Any decrease in expenditures by healthcare facilities or increased financing costs could decrease demand for our medication and supply dispensing systems and related services and reduce our revenues.

Changing customer requirements could decrease the demand for our products and services and our new product solutions may not achieve market acceptance.

The medication management and supply chain solutions market is characterized by evolving technologies and industry standards, frequent new product introductions and dynamic customer requirements that may render existing products obsolete or less competitive. The medication management and supply chain solutions market could erode rapidly due to unforeseen changes in the features and functions of competing products, as well as the pricing models for such products. Our future success will depend in part upon our ability to enhance our existing products and services and to develop and introduce new products and services to meet changing customer requirements. The process of developing products and services such as those we offer is extremely complex and is expected to become increasingly more complex and expensive in the future as new technologies are introduced. If we are unable to enhance our existing products or develop new products to meet changing customer requirements, and bring such enhancements and products to market in a timely manner, demand for our products could decrease.

We cannot provide assurance that we will be successful in marketing any new products or services that we introduce, that new products or services will compete effectively with similar products or services sold by our competitors, or that the level of market acceptance of such products or services will be sufficient to generate expected revenues and synergies with our other products or services. Deployment of new products or services often requires interoperability with other Omnicell products or services as well as with healthcare facilities' existing information management systems. If these products or services fail to satisfy these demanding technological objectives, our customers may be dissatisfied and we may be unable to generate future sales.

The healthcare industry faces financial constraints and consolidation that could adversely affect the demand for our products and services.

The healthcare industry has faced, and will likely continue to face, significant financial constraints. Recently enacted legislation such as the American Recovery and Reinvestment Act in 2009, the Patient Protection and Affordable Care Act in 2010, the Budget Control Act of 2011, and other health reform legislation may cause customers to postpone purchases of our products while the impact of this legislation on their operations is determined. Our automation solutions often involve a significant financial commitment from our customers and, as a result, our ability to grow our business is largely dependent on our customers' capital and operating budgets. To the extent healthcare spending declines or increases more slowly than we anticipate, demand for our products and services could decline.

Many healthcare providers have consolidated to create larger healthcare delivery organizations in order to achieve greater market power. If this consolidation continues, it would increase the size of certain target customers, which could increase the cost, effort and difficulty in selling our products to such target customers, or could cause our existing customers or potential new customers to begin utilizing our competitors' products if such customers are acquired by healthcare providers that prefer our competitors' products to ours. In addition, the resulting organizations could have greater bargaining power, which may lead to price erosion.

If we experience delays in installations of our medication and supply dispensing systems or our more complex medication packaging systems, resulting in delays in our ability to recognize revenue, our competitive position, results of operations and financial condition could be harmed.

The purchase of our medication and supply dispensing systems or our more complex medication packaging systems is often part of a customer's larger initiative to re-engineer its pharmacy, distribution and materials management systems and as a result, our sales cycles are often lengthy. The purchase of our systems often entail larger strategic purchases by customers that frequently require more complex and stringent contractual requirements and generally involve a significant commitment of management attention and resources by prospective customers. These larger and more complex transactions often require the input and approval of many decision-makers, including pharmacy directors, materials managers, nurse managers, financial managers, information systems managers, administrators, lawyers and boards of directors. For these and other reasons, the sales cycle associated with the sale of our medication and supply dispensing systems is often lengthy and subject to a number of delays over which we have little or no control. A delay in, or loss of, sales of our medication and supply dispensing systems could have an adverse effect upon our operating results and could harm our business.

In addition, and in part as a result of the complexities inherent in larger transactions, the average time between the purchase and installation of our systems is generally between two weeks and one year. Delays in installation can occur for reasons that are often outside of our control. We have also experienced fluctuations in our customer and transaction size mix, which makes our ability to forecast our product backlog more difficult. Because we recognize revenue for our medication and supply dispensing systems and our more complex medication packaging systems only upon installation at a customer's site, any delay in installation by our customers will also cause a delay in the recognition of the revenue for that system.

We may not be able to successfully integrate acquired businesses or technologies into our existing business, which could negatively impact our operating results.

As a part of our business strategy we may seek to acquire businesses, technologies or products in the future. For example, in 2012 we completed the acquisition of MTS. We cannot provide assurance that any acquisition or any future transaction we complete will result in long-term benefits to us or our stockholders, or that our management will be able to integrate or manage the acquired business effectively. Acquisitions entail numerous risks, including difficulties associated with the integration of operations, technologies, products and personnel that, if realized, could harm our operating results. Risks related to potential acquisitions include, but are not limited to:

- difficulties in combining previously separate businesses into a single unit and the complexity of managing a more dispersed organization as sites are acquired;

- the substantial costs that may be incurred and the substantial diversion of management's attention from day-to-day business when evaluating and negotiating such transactions and then integrating an acquired business;

- discovery, after completion of the acquisition, of liabilities assumed from the acquired business or of assets acquired that are broader in scope and magnitude or are more difficult to manage than originally assumed;

- failure to achieve anticipated benefits such as cost savings and revenue enhancements;
- difficulties related to assimilating the products or key personnel of an acquired business; and
- failure to understand and compete effectively in markets in which we have limited previous experience.

Successful integration of acquired operations, products and personnel into Omnicell may place a significant burden on the combined company's management and internal resources. We may also experience difficulty in effectively integrating the different cultures and practices of any acquired entity. The challenges of integrating acquired entities could disrupt the combined company's ongoing business, distract its management focus from other opportunities and challenges, and increase expenses and working capital requirements. The diversion of management attention and any difficulties encountered in the transition and integration process could harm our business, financial condition and operating results.

Demand for our consumable medication packages is time-sensitive and if we are not able to supply the demand from our institutional and retail pharmacy customers on schedule and with quality packaging products, they may utilize alternative means to distribute medications to their customers.

Approximately 21% of our revenue is generated from the sale of consumable medication packages, which are produced in our St. Petersburg, Florida facilities on a continuous basis and shipped to our institutional pharmacies and retail pharmacy customers shortly before they are required by those customers. The demands placed on institutional pharmacies and retail pharmacies by their customers represent real time requirements of those customers. Our customer agreements for the sale of consumable medication packages are typically short-term in nature and typically do not include any volume commitments on the part of the customer. Although our packaging may be considered the preferred method of maintaining control of medications during the medication distribution and administration process, institutional and retail pharmacies have alternative methods of distributing medications, including bulk and alternative packaging, and medication adherence packaging may be supplied by our competitors. To the extent that we are unable to supply quality packaging to our customers in a timely manner, that demand will be met via alternative distribution methods, including consumable medication packaging sold by our competitors, and our revenue will decline. Any disruption in the production capabilities of our St. Petersburg facilities will adversely affect our ability to ship our consumable medication packages and would reduce our revenue.

Our international operations may subject us to additional risks that can adversely affect our operating results.

We currently have operations outside of the United States, including sales efforts centered in Canada, Europe, the Middle East and Asia-Pacific regions and supply chain efforts in Asia. In 2011, we launched Mandarin-language versions of our G4 medication automation products for clinical use in China and entered into a partnership to distribute, install, and service our automated medication dispensing systems in China. We intend to continue to expand our international operations, particularly in certain markets that we view as strategic, including China and the Middle East. Our international operations subject us to a variety of risks, including:

- our reliance on distributors for the sale and post-sale support of our automated dispensing systems outside the United States;
- the difficulty of managing an organization operating in various countries;
- growing political sentiment against international outsourcing of production;
- reduced protection for intellectual property rights, particularly in jurisdictions that have less developed intellectual property regimes;
- changes in foreign regulatory requirements;
- the requirement to comply with a variety of international laws and regulations, including privacy, labor, import, export, tax, anti-bribery and employment laws and changes in tariff rates;
- fluctuations in currency exchange rates and difficulties in repatriating funds from certain countries;
- additional investment, coordination and lead-time necessary to successfully interface our automation solutions with the existing information systems of our customers or potential customers outside of the United States; and
- political unrest, terrorism and the potential for other hostilities in areas in which we have facilities.

If we are unable to anticipate and address these risks properly, our business or operating results will be harmed.

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Government regulation of the healthcare industry could reduce demand for our products, or substantially increase the cost to produce our products.

The manufacture and sale of our current products are not regulated by the United States Food and Drug Administration (the "FDA"), or the Drug Enforcement Administration (the "DEA"). However, our current products, and any future products, may be regulated in the future by these or other federal agencies due to future legislative and regulatory initiatives or reforms. Direct regulation of our business and products by the FDA, DEA or other federal agencies could substantially increase the cost to produce our products and increase the time required to bring those products to market, reduce the demand for our products and reduce our revenues. In addition, healthcare providers and facilities that use our equipment and dispense controlled substances are subject to regulation by the DEA. The failure of these providers and facilities to comply with DEA requirements, including the Controlled Substances Act and its implementing regulations, could reduce demand for our products and harm our competitive position, results of operations and financial condition. Pharmacies are regulated by individual state boards of pharmacy that issue rules for pharmacy licensure in their respective jurisdictions. State boards of pharmacy do not license or approve our medication and supply dispensing systems; however, pharmacies using our equipment are subject to state board approval. The failure of such pharmacies to meet differing requirements from a significant number of state boards of pharmacy could decrease demand for our products and harm our competitive position, results of operations and financial condition. Similarly, hospitals must be accredited by The Joint Commission in order to be eligible for Medicaid and Medicare funds. The Joint Commission does not approve or accredit medication and supply dispensing systems; however, disapproval of our customers' medication and supply dispensing management methods and their failure to meet The Joint Commission requirements could decrease demand for our products and harm our competitive position, results of operations and financial condition.

While we have implemented a Privacy and Use of Information Policy and adhere to established privacy principles, use of customer information guidelines and related federal and state statutes, we cannot assure you that we will be in compliance with all federal and state healthcare information privacy and security laws that we are directly or indirectly subject to, including, without limitation, the Health Insurance Portability and Accountability Act of 1996, or ("HIPAA"). Among other things, this legislation required the Secretary of Health and Human Services ("HHS") to adopt national standards governing the conduct of certain electronic health information transactions and protecting the privacy and security of personally identifiable health information maintained or transmitted by "covered entities," which include pharmacies and other healthcare providers with which we do business.

The standards adopted to date include, among others, the "Standards for Privacy of Individually Identifiable Health Information," which restrict the use and disclosure of personally identifiable health information by covered entities, and the "Security Standards," which require covered entities to implement administrative, physical and technical safeguards to protect the integrity and security of certain electronic health information. Under HIPAA, we are considered a "business associate" in relation to many of our customers that are covered entities, and as such, most of these customers have required that we enter into written agreements governing the way we handle and safeguard certain patient health information we may encounter in providing our products and services and may impose liability on us for failure to meet our contractual obligations. Further, pursuant to changes in HIPAA under the American Recovery and Reinvestment Act of 2009 ("ARRA"), we are now also covered under HIPAA similar to other covered entities and in some cases, subject to the same civil and criminal penalties as a covered entity. A number of states have also enacted privacy and security statutes and regulations that, in some cases, are more stringent than HIPAA and may also apply directly to us. If our past or present operations are found to violate any of these laws, we may be subject to fines, penalties and other sanctions.

During November 2012, an Omnicell electronic device containing medication dispensing cabinet log files from three health system customers was stolen from an Omnicell employee's locked vehicle. The files on this device contained certain protected patient health information related to medication dispensing transactions from our medication dispensing cabinets over a one to three-week period, downloaded by the employee while troubleshooting software for the hospitals. As a result of this unauthorized disclosure of personal health information, we may experience contractual indemnification obligations under business associate agreements with certain customers, reputational harm and a reduction in demand from our customers. To the extent that this disclosure is deemed to be a violation of

HIPAA or other privacy or security laws, we may be subject to significant fines, penalties and other sanctions.
On March 8, 2013, a putative class action complaint was filed against us and certain of our customers in the United States District Court for the District of New Jersey 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, described above and subsequent notification of this unauthorized disclosure of personal health information. The plaintiff 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. This matter is further described under "Legal Proceedings" in Note 11 of Notes to Consolidated Financial Statements in Part I, Item 1, of this Quarterly Report on Form 10-Q and Omnicell intends to defend the matter vigorously.

In addition, we cannot predict the potential impact of future HIPAA standards and other federal and state privacy and security laws that may be enacted at any time on our customers or on Omnicell. These laws could restrict the ability of our customers to obtain, use or disseminate patient information, which could reduce the demand for our products or force us to redesign our products in order to meet regulatory requirements.

Covenants in the credit agreement restrict our business and operations in many ways and if we do not effectively manage our compliance with these covenants, our financial conditions and results of operations could be adversely affected

On September 25, 2013, we entered into a $75.0 million revolving credit facility pursuant to a Credit Agreement, by and among Omnicell, Wells Fargo Bank, National Association, as administrative agent, and the lenders from time to time party thereto (the “Credit Agreement”). The Credit Agreement contains various customary covenants that limit our ability and/or our subsidiaries’ ability to, among other things:

- incur or assume liens or additional debt or provide guarantees in respect of obligations or other persons;
- issue redeemable preferred stock;
- pay dividends or distributions or redeem or repurchase capital stock;
- prepay, redeem or repurchase certain debt;
- make loans, investments, acquisitions (including acquisitions of exclusive licenses) and capital expenditures;
- enter into agreements that restrict distributions from our subsidiaries;
- sell assets and capital stock of our subsidiaries;
- enter into certain transactions with affiliates; and
- consolidate or merge with or into, or sell substantially all of our assets to, another person.

The Credit Agreement also includes, among other financial covenants, financial covenants that require us to maintain a maximum total leverage ratio and minimum fixed charge coverage ratio. Our ability to comply with these financial covenants may be affected by events beyond our control. Our failure to comply with any of the covenants could result in a default under the Credit Agreement, which could permit the administrative agent or the lenders to declare all or part of any outstanding borrowings to be immediately due and payable, or to refuse to permit additional borrowings under the revolving credit facility, which could restrict our operations, particularly our ability to respond to changes in our business or to take specified actions to take advantage of certain business opportunities that may be presented to us. In addition, if we are unable to repay those amounts, the administrative agent and the lenders under the Credit Agreement could proceed against the collateral granted to them to secure that debt, which would seriously harm our business.

If we are unable to recruit and retain skilled and motivated personnel, our competitive position, results of operations and financial condition could be harmed.

Our success is highly dependent upon the continuing contributions of our key management, sales, technical and engineering staff. We believe that our future success will depend upon our ability to attract, train and retain highly skilled and motivated personnel. As more of our products are installed in increasingly complex environments, greater technical expertise will be required. As our installed base of customers increases, we will also face additional demands on our customer service and support personnel, requiring additional resources to meet these demands. We may experience difficulty in recruiting qualified personnel. Competition for qualified technical, engineering, managerial, sales, marketing, financial reporting and other personnel can be intense and may not be successful in attracting and retaining qualified personnel. Competitors have in the past attempted, and may in the future attempt, to recruit our employees.

In addition, we have historically used stock options, restricted stock units and other forms of equity compensation as key components of our employee compensation program in order to align employees' interests with the interests of our stockholders, encourage employee retention and provide competitive compensation packages. The effect of managing share-based compensation expense may make it less favorable for us to grant stock options, restricted stock units or other forms of equity compensation, to employees in the future. In order to continue granting equity compensation at competitive levels, we must seek stockholder approval for any increases to the number of shares reserved for issuance under our equity incentive plans, such as the share increase for which we obtained approval at our 2013 Annual Meeting of Stockholders, and we cannot assure you that we will receive such approvals in the future. Any failure to receive approval for current or future proposed increases could prevent us from granting equity compensation at competitive levels and make it more difficult to attract, retain and motivate employees. Further, to the extent that we expand our business or product lines through the acquisition of other businesses, any failure to receive any such approvals could prevent us from securing employment commitments from such newly acquired employees. Failure to attract and retain key personnel could harm our competitive position, results of operations and financial condition.

In the past, we have experienced substantial fluctuations in customer demand, and we cannot be sure that we will be able to respond proactively to future changes in customer demand.

Our ability to adjust to fluctuations in our revenue while still achieving or sustaining profitability is dependent upon our ability to manage costs and control expenses. If macroeconomic and general market conditions improve and return to historical levels, our ability to grow revenue and profitability will also be dependent on our ability to continue to manage costs and control expenses. If our revenue increases rapidly, we may not be able to manage this growth effectively. Future growth is dependent on the continued demand for our products, the volume of installations we are able to complete, our ability to continue to meet our customers' needs and provide a quality installation experience and our flexibility in manpower allocations among customers to complete installations on a timely basis.

Regarding our expenses, our ability to control expense is dependent on our ability to continue to develop and leverage effective and efficient human and information technology systems, our ability to gain efficiencies in our workforce through the local and worldwide labor markets and our ability to grow our outsourced vendor supply model. Our expense growth rate may equal or exceed our revenue growth rate if we are unable to streamline our operations, or fail to reduce the costs or increase the margins of our products. In addition, we may not be able to reduce our expenses to keep pace with any reduction in our revenue, which could harm our results of operations and financial position.

Our failure to protect our intellectual property rights could negatively affect our ability to compete.

Our success depends in part on our ability to obtain patent protection for technology and processes and our ability to preserve our trademarks, copyrights and trade secrets. We have pursued patent protection in the United States and foreign jurisdictions for technology that we believe to be proprietary and for technology that offers us a potential competitive advantage for our products. We intend to continue to pursue such protection in the future. Our issued patents relate to various features of our medication and supply dispensing systems and our packaging systems. We cannot assure you that we will file any patent applications in the future, and that any of our patent applications will result in issued patents or that, if issued, such patents will provide significant protection for our technology and processes. Furthermore, we cannot assure you that others will not develop technologies that are similar or superior to our technology or that others will not design around the patents we own. All of our system software is copyrighted and subject to the protection of applicable copyright laws. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or obtain and use information that we regard as proprietary, which could harm our competitive position.

Our quarterly operating results may fluctuate and may cause our stock price to decline.

Our quarterly operating results may vary in the future depending on many factors that include, but are not limited to, the following:

- our ability to successfully install our products on a timely basis and meet other contractual obligations necessary to recognize revenue;
- the size, product mix and timing of orders for our medication and supply dispensing systems, and our medication packaging systems, and their installation and integration;
- the overall demand for healthcare medication management and supply chain solutions;
- changes in pricing policies by us or our competitors;
- the number, timing and significance of product enhancements and new product announcements by us or our competitors;
- the timing and significance of any acquisition or business development transactions that we may consider or negotiate and the revenues, costs and earnings that may be associated with these transactions;
- the relative proportions of revenues we derive from products and services;
- fluctuations in the percentage of sales attributable to our international business;
- our customers' budget cycles;
- changes in our operating expenses and our ability to stabilize expenses;
- our ability to generate cash from our accounts receivable on a timely basis;
- the performance of our products;

- changes in our business strategy;
- macroeconomic and political conditions, including fluctuations in interest rates, tax increases and availability of credit markets; and
- volatility in our stock price and its effect on equity-based compensation expense.

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Due to all of these factors, our quarterly revenues and operating results are difficult to predict and may fluctuate, which in turn may cause the market price of our stock to decline.

If we are unable to maintain our relationships with group purchasing organizations or other similar organizations, we may have difficulty selling our products and services to customers represented by these organizations.

A number of group purchasing organizations, including AmeriNet, Inc., Carolina Shared Services, LLC, Child Health Corporation of America, HealthTrust Purchasing Group, L.P., MedAssets, Inc. Supply Chain Systems, Novation, LLC, Premier Purchasing Partners, L.P. and Resources Optimization & Innovation, LLC have negotiated standard contracts for our products on behalf of their member healthcare organizations. Members of these group purchasing organizations may purchase under the terms of these contracts, which obligate us to pay the group purchasing organization a fee. We have also contracted with the United States General Services Administration, allowing the Department of Veteran Affairs, the Department of Defense and other Federal Government customers to purchase our products. These contracts enable us to more readily sell our products and services to customers represented by these organizations. Some of our contracts with these organizations are terminable at the convenience of either party. The loss of any of these relationships could impact the breadth of our customer base and could impair our ability to meet our revenue targets or increase our revenues. These organizations may not renew our contracts on similar terms, if at all, and they may choose to terminate our contracts before they expire, any of which could cause our revenues to decline.

If we are unable to maintain our relationships with major institutional pharmacies, we may experience a decline in the sales of blister cards and other consumables sold to these customers.

The institutional pharmacy market consists of significant national suppliers of medications to non-acute care facilities, smaller regional suppliers, and very small local suppliers. Although none of these customers comprised more than 10% of our revenues as of September 30, 2013, they may, in some periods, comprise between 5% and 10% of our revenues. If these larger national suppliers were to purchase consumable blister card components from alternative sources, or if alternatives to blister cards were used for medication control, our revenues would decline.

Our failure to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act of 2002 could cause our stock price to decline.

Section 404 of the Sarbanes-Oxley Act of 2002 and the related rules and regulations of the SEC require annual management assessments of the effectiveness of our internal control over financial reporting and a report by our independent registered public accounting firm attesting to the effectiveness of internal control. If we fail to maintain effective internal control over financial reporting, as such standards are modified, supplemented or amended from time to time, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal control over financial reporting.

If the market price of our common stock continues to be highly volatile, the investment value of our common stock may decline.

During the nine months ended September 30, 2013, our common stock traded between $14.68 and $25.22 per share. The market price for shares of our common stock has been and may continue to be highly volatile. In addition, our announcements or external events may have a significant impact on the market price of our common stock. These announcements or external events may include:

- changes in our operating results;
- developments in our relationships with corporate customers;
- changes in the ratings of our common stock by securities analysts;
- announcements by us or our competitors of technological innovations or new products;
- announcements by us or our competitors of acquisitions of businesses, products or technologies; or
- general economic and market conditions.

Furthermore, the stock market as a whole from time to time has experienced extreme price and volume fluctuations, which have particularly affected the market prices for technology companies. These broad market fluctuations may cause the market price of our common stock to decline irrespective of our performance. In addition, sales of substantial amounts of our common stock in the public market could lower the market price of our common stock.

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We depend on a limited number of suppliers for our products and our business may suffer if we were required to change suppliers to obtain an adequate supply of components, equipment and raw materials on a timely basis.
Although we generally use parts and components for our products with a high degree of modularity, certain components are presently available only from a single source or limited sources. We rely on a limited number of suppliers for the raw materials that are necessary in the production of our consumable medication packages. We have generally been able to obtain adequate supplies of all components and raw materials in a timely manner from existing sources, or where necessary, from alternative sources of supply. We engage multiple single source third-party manufacturers to build several of our sub-assemblies. The risk associated with changing to alternative vendors, if necessary, for any of the numerous components used to manufacture our products could limit our ability to manufacture our products and harm our business. Our reliance on a few single source partners to build our hardware sub-assemblies and on a limited number of suppliers for the raw materials that are necessary in the production of our consumable medication packages, a reduction or interruption in supply from our partners or suppliers, or a significant increase in the price of one or more components could have an adverse impact on our business, operating results and financial condition. In certain circumstances, the failure of any of our suppliers or us to perform adequately could result in quality control issues affecting end users' acceptance of our products. These impacts could damage customer relationships and could harm our business.

Our U.S. government lease agreements are subject to annual budget funding cycles and mandated unilateral changes, which may affect our ability to enter into such leases or to recognize revenue and sell receivables based on these leases.

U.S. government customers that lease our equipment typically sign contracts with five-year payment terms that are subject to one-year government budget funding cycles. Further, the government has in certain circumstances mandated unilateral changes in its Federal Supply Services contract that could render our lease terms with the government less attractive. In our judgment and based on our history with these accounts, we believe these receivables are collectible. However, in the future, the failure of any of our U.S. government customers to receive their annual funding, or the government mandating changes to the Federal Supply Services contract could impair our ability to sell lease equipment to these customers or to sell our U.S. government receivables to third-party leasing companies. In addition, the ability to collect payments on unsold receivables could be impaired and may result in a write-down of our unsold receivables from U.S. government customers. As of September 30, 2013, the balance of our unsold leases to U.S. government customers was $14.1 million.

If we fail to manage our inventory properly, our revenue, gross margin and profitability could suffer.

Managing our inventory of components and finished products is a complex task. A number of factors, including, but not limited to, the need to maintain a significant inventory of certain components that are in short supply or that must be purchased in bulk to obtain favorable pricing, the general unpredictability of demand for specific products and customer requests for quick delivery schedules, may result in us maintaining large amounts of inventory. Other factors, including changes in market demand, customer requirements and technology, may cause our inventory to become obsolete. Any excess or obsolete inventory could result in inventory write-downs, which in turn could harm our business and results of operations.

If we are unable to successfully interface our automation solutions with the existing information systems of our customers, they may choose not to use our products and services.

For healthcare facilities to fully benefit from our automation solutions, our systems must interface with their existing information systems. This may require substantial cooperation, incremental investment and coordination on the part of our customers and may require coordination with third-party suppliers of the existing information systems. There is little uniformity in the systems currently used by our customers, which complicates the interfacing process. If these systems are not successfully interfaced, our customers could choose not to use or to reduce their use of our automation solutions, which would harm our business.

Additionally, our competitors may enter into agreements with providers of hospital information management systems that are designed to increase the interoperability of their respective products. To the extent our competitors are able to increase the interoperability of their products with those of the major hospital information systems providers, customers who utilize such information systems may choose not to use our products and services.

Intellectual property claims against us could harm our competitive position, results of operations and financial condition.

We expect that developers of medication and supply dispensing systems and medication packaging systems, will be increasingly subject to infringement claims as the number of products and competitors in our industry grows and the functionality of products in different industry segments overlaps. In the future, third parties may claim that we have infringed upon their intellectual property rights with respect to current or future products. We do not carry special insurance that covers intellectual property infringement claims; however, such claims may be covered under our traditional insurance policies. These policies contain terms, conditions and exclusions that make recovery for intellectual property infringement claims difficult to guarantee. Any infringement claims, with or without merit, could be time-consuming to defend, result in costly litigation, divert management's attention and resources, cause product shipment delays or require us to enter into royalty or licensing agreements. These royalty or licensing agreements, if required, may not be available on terms acceptable to us, or at all, which could harm our competitive position, results of operations and financial condition.

Our software products are complex and may contain defects, which could harm our reputation, results of operations and financial condition.

We market products that contain software and products that are software only. Although we perform extensive testing prior to releasing software products, these products may contain undetected errors or bugs when first released. These may not be discovered until the product has been used by customers in different application environments. Failure to discover product deficiencies or bugs could require design modifications to previously shipped products or cause delays in the installation of our products and unfavorable publicity or negatively impact system shipments, any of which could harm our business, financial condition and results of operations.

Product liability claims against us could harm our competitive position, results of operations and financial condition.

Our products provide medication management and supply chain management solutions for the healthcare industry. Despite the presence of healthcare professionals as intermediaries between our products and patients, if our products fail to provide accurate and timely information or operate as designed, customers, patients or their family members could assert claims against us for product liability. Moreover, failure of health-care facility employees to use our products for their intended purposes could result in product liability claims against us. Litigation with respect to product liability claims, regardless of any outcome, could result in substantial cost to us, divert management's attention from operations and decrease market acceptance of our products. We possess a variety of insurance policies that include coverage for general commercial liability, technology errors and omissions liability and we attempt to mitigate these risks through contractual terms negotiated with our customers. However, these policies and protective contractual terms may not be adequate against product liability claims. A successful claim brought against us, or any claim or product recall that results in negative publicity about us, could harm our competitive position, results of operations and financial condition. Also, in the event that any of our products is defective, we may be required to recall or redesign those products.

We are dependent on technologies provided by third-party vendors, the loss of which could negatively and materially affect our ability to market, sell, or distribute our products.

Some of our products incorporate technologies owned by third parties that are licensed to us for use, modification, and distribution. If we lose access to third-party technologies, or we lose the ongoing rights to modify and distribute these technologies with our products, we will either have to devote resources to independently develop, maintain and support the technologies ourselves, pay increased license costs, or transition to another vendor. Any independent development, maintenance or support of these technologies by us or the transition to alternative technologies could be costly, time consuming and could delay our product releases and upgrade schedules. These factors could negatively and materially affect our ability to market, sell or distribute our products.

Complications in connection with our ongoing business information system upgrades, including those required to adopt new accounting standards and eventually adopt changes driven by converged accounting standards for revenues, leases and other topics, may impact our results of operations, financial condition and cash flows.

We continue to upgrade our enterprise-level business information system with new capabilities. Based upon the complexity of some of the upgrades, there is risk that we will not see the expected benefit from the implementation of these upgrades in accordance with their anticipated timeline and will incur costs in addition to those we have already planned for. In addition, in future years, we may need to begin efforts to comply with final converged accounting standards to be established by the Financial Accounting Standards Board ("FASB") and the International Accounting Standards Board ("IASB") for revenues, leases and other components of our financial reporting. These new standards could require us to modify our accounting policies, including our revenue recognition policy, which we modified in fiscal 2011. We further anticipate that integration of these and possibly other new standards may require a substantial amount of management's time and attention and require integration with our enterprise resource planning system. The implementation of the system and the adoption of future new standards, in isolation as well as together, could result in operating inefficiencies and financial reporting delays, and could impact our ability to record certain business transactions timely. All of these potential results could adversely impact our results of operations, financial condition and cash flows.

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Outstanding employee stock options have the potential to dilute stockholder value and cause our stock price to decline.

We grant stock options to certain of our employees as incentives to join Omnicell or as an on-going reward and retention vehicle. At September 30, 2013, we had options outstanding to purchase approximately 3.2 million shares of our common stock at exercise prices ranging from $6.40 to $29.16 per share, at a weighted-average exercise price of $15.07 per share. If some or all of these shares are sold into the public market over a short time period, the price of our common stock may decline, as the market may not be able to absorb those shares at the prevailing market prices. Such sales may also make it more difficult for us to sell equity securities in the future on terms that we deem acceptable.

Changes in our tax rates, the adoption of new tax legislation or exposure to additional tax liabilities could affect our future results.

We are subject to taxes in the United States and other foreign jurisdictions. Our future effective tax rates could be affected by several factors, many of which are outside of our control, including; changes in the mix of earnings with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, or changes in tax laws, the timing of such changes, or their interpretation. We regularly assess the likelihood of adverse outcomes to determine the adequacy of our provision for taxes. We are also subject to examination of our income tax returns by the Internal Revenue Service and other tax authorities. There can be no assurance that the outcomes from these examinations will not materially adversely affect our financial condition and operating results.

Catastrophic events may disrupt our business and harm our operating results.

We rely on our network infrastructure, data centers, enterprise applications, and technology systems for the development, marketing, support and sales of our products, and for the internal operation of our business. These systems are susceptible to disruption or failure in the event of a major earthquake, fire, flood, cyber-attack, terrorist attack, telecommunications failure, or other catastrophic event. Many of these systems are housed or supported in or around our corporate headquarters located in Northern California, near major earthquake faults, and where a significant portion of our research and development activities and other critical business operations take place. Other critical systems, including our manufacturing facilities for our consumable medication packages, are housed in St. Petersburg, Florida in communities that have been subject to significant tropical storms. Disruptions to or the failure of any of these systems, and the resulting loss of critical data, which is not quickly recoverable by the effective execution of disaster recovery plans designed to reduce such disruption, could cause delays in our product development, prevent us from fulfilling our customers' orders, and could severely affect our ability to conduct normal business operations, the result of which would adversely affect our operating results.

Anti-takeover provisions in our charter documents and under Delaware law, and any stockholders' rights plan we may adopt in the future, make an acquisition of us, which may be beneficial to our stockholders, more difficult.

We are incorporated in Delaware. Certain anti-takeover provisions of Delaware law and our charter documents as currently in effect may make a change in control of our company more difficult, even if a change in control would be beneficial to the stockholders. Our anti-takeover provisions include provisions in our certificate of incorporation providing that stockholders' meetings may only be called by our Board of Directors and provisions in our bylaws providing that the stockholders may not take action by written consent and requiring that stockholders that desire to nominate any person for election to our Board of Directors or to make any proposal with respect to business to be conducted at a meeting of our stockholders be submitted in appropriate form to our Secretary within a specified period of time in advance of any such meeting. Delaware law also prohibits corporations from engaging in a business combination with any holders of 15% or more of their capital stock until the holder has held the stock for three years unless, among other possibilities, our Board of Directors approves the transaction. Our Board of Directors may use these provisions to prevent changes in the management and control of our company. Also, under applicable Delaware law, our board of directors may adopt additional anti-takeover measures in the future.

The stockholder rights plan adopted by our Board of Directors in February 2003 expired by its terms in February 2013. Our Board of Directors could adopt a similar plan in the future if it determines that such action is in the best interests of our stockholders. Such a plan may have the effect of discouraging, delaying or preventing a change in control of our company that may be beneficial to our stockholders.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Item 5. OTHER INFORMATION

None.

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Item 6. EXHIBITS

Exhibit Number	Exhibit Description	Incorporation By Reference Form	SEC File No.	Exhibit	Filing Date
3.1	Amended and Restated Certificate of Incorporation of Omnicell, Inc.	S-1	333-57024	3.1	3/14/2001
3.2	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of Omnicell, Inc.	10-Q	000-33043	3.2	8/9/2010
3.3	Certificate of Designation of Series A Junior Participating Preferred Stock	10-K	000-33043	3.2	3/28/2003
3.4	Bylaws of Omnicell, Inc., as amended	10-Q	000-33043	3.3	8/9/2007
4.1	Reference is made to Exhibits 3.1, 3.2 , 3.3 and 3.4				
4.2	Form of Common Stock Certificate	S-1	333-57024	4.1	3/14/2001
10.1	Credit Agreement, dated as of September 25, 2013, among Omnicell, Inc., the Lender party thereto, and Wells Fargo Bank, National Association	8-K	000-33043	10.1	9/26/2013
31.1+	Certification of Chief Executive Officer, as required by Rule 13a-14(a) or Rule 15d-14(a)				
31.2+	Certification of Chief Financial Officer, as required by Rule 13a-14(a) or Rule 15d-14(a)				
32.1+	Certification of Chief Executive Officer, as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350)(1)				
32.2+	Certification of Chief Financial Officer, as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350)(1)				
101.INS+	XBRL Instance Document				
101.SCH+	XBRL Taxonomy Extension Schema Document				
101.CAL+	XBRL Taxonomy Extension Calculation Linkbase Document				

101.DEF+	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB+	XBRL Taxonomy Extension Labels Linkbase Document

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101.PRE+	XBRL Taxonomy Extension Presentation Linkbase Document

+ Filed herewith

(1) This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of the Registrant under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

OMNICELL, INC.

Date: November 8, 2013

/s/ ROBIN G. SEIM
Robin G. Seim
Chief Financial Officer and Executive Vice President
Finance, Administration and Manufacturing

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