VOCERA COMMUNICATIONS, INC.
Form 10-Q
November 14, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2013
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period from to
Commission File Number: 001-35469

VOCERA COMMUNICATIONS, INC.
(Exact name of registrant as specified in its charter)

Delaware	94-3354663
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Vocera Communications, Inc.
525 Race Street
San Jose, CA 95126
(408) 882-5100
(Address and telephone number of principal executive offices)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at November 6, 2013

Common Stock, $0.0003 par value per share	24,892,350

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FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2013
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PART I: FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)
Vocera Communications, Inc.
Condensed Consolidated Balance Sheets
(In Thousands, Except Share and Par Amounts)
(Unaudited)

	September 30, 2013	December 31, 2012
Assets		
Current assets		
Cash and cash equivalents	$18,285	$92,521
Short-term investments	106,947	34,989
Accounts receivable, net of allowance	20,260	21,697
Other receivables	954	550
Inventories	4,798	2,772
Prepaid expenses and other current assets	2,517	2,808
Total current assets	153,761	155,337
Property and equipment, net	5,651	3,631
Intangible assets, net	1,725	2,267
Goodwill	5,575	5,575
Other long-term assets	783	495
Total assets	$167,495	$167,305
Liabilities and stockholders' equity		
Current liabilities		
Accounts payable	$2,963	$2,854
Accrued payroll and other current liabilities	8,616	11,754
Deferred revenue, current	23,982	22,451
Total current liabilities	35,561	37,059
Deferred revenue, long-term	6,066	5,882
Other long-term liabilities	1,672	1,239
Total liabilities	43,299	44,180
Commitments and contingencies (Note 7)		
Stockholders' equity		
Preferred stock, $0.0003 par value - 5,000,000 shares authorized as of September 30, 2013 and December 31, 2012; zero shares issued and outstanding	—	—
Common stock, $0.0003 par value - 100,000,000 shares authorized as of September 30, 2013 and December 31, 2012; 24,866,334 and 24,229,356 shares issued and outstanding as of September 30, 2013 and December 31, 2012, respectively	8	7
Additional paid-in capital	186,777	177,081
Accumulated other comprehensive income	2	5
Accumulated deficit	(62,591)	(53,968)
Total stockholders’ equity	124,196	123,125
Total liabilities and stockholders’ equity	$167,495	$167,305

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

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Vocera Communications, Inc.
Condensed Consolidated Statements of Operations
(In Thousands, Except Per Share Amounts)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Revenue				
Product	$15,666	$16,851	$43,966	$47,643
Service	10,401	9,117	29,810	26,322
Total revenue	26,067	25,968	73,776	73,965
Cost of revenue				
Product	5,635	5,237	15,581	16,138
Service	4,155	3,743	12,409	11,134
Total cost of revenue	9,790	8,980	27,990	27,272
Gross profit	16,277	16,988	45,786	46,693
Operating expenses				
Research and development	3,798	3,043	10,830	8,248
Sales and marketing	11,791	8,532	32,702	24,064
General and administrative	4,073	3,745	11,000	10,449
Total operating expenses	19,662	15,320	54,532	42,761
(Loss) income from operations	(3,385)	1,668	(8,746)	3,932
Interest income	87	60	170	86
Interest expense and other finance charges	—	—	—	(74)
Other (expense) income, net	76	50	(55)	(1,442)
(Loss) income before income taxes	(3,222)	1,778	(8,631)	2,502
Benefit from (provision for) income taxes	120	(41)	8	(420)
Net (loss) income	(3,102)	1,737	(8,623)	2,082
Less: undistributed earnings attributable to participating securities	—	(9)	—	(1,299)
Net (loss) income attributable to common stockholders	$(3,102)	$1,728	$(8,623)	$783
Net (loss) income per share attributable to common stockholders				
Basic	$(0.13)	$0.08	$(0.35)	$0.05
Diluted	$(0.13)	$0.07	$(0.35)	$0.04
Weighted average shares used to compute net (loss) income per share attributable to common stockholders				
Basic	24,747	22,450	24,530	15,973
Diluted	24,747	25,337	24,530	18,751

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

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Vocera Communications, Inc.
Condensed Consolidated Statements of Comprehensive Income (Loss)
(In Thousands)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Net (loss) income	$(3,102)	$1,737	$(8,623)	$2,082
Other comprehensive income (loss), net:				
Change in unrealized gain (loss) on investments, net	89	110	(3)	(81)
Comprehensive (loss) income	$(3,013)	$1,847	$(8,626)	$2,001

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

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Vocera Communications, Inc.
Condensed Consolidated Statements of Cash Flows
(In Thousands)
(Unaudited)

	Nine months ended September 30, 2013	2012
Cash flows from operating activities		
Net (loss) income	$(8,623)	$2,082
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	1,798	1,932
Change in non-cash interest	(52)	(39)
Loss on disposal of property and equipment	—	2
Allowance for doubtful accounts	14	—
Inventory write-down	136	207
Change in lease-related performance liabilities	(104)	—
Stock-based compensation expense	6,113	2,671
Excess tax benefits from employee stock plans	—	(300)
Change in fair value of warrant liability	—	1,631
Changes in operating assets and liabilities:		
Accounts receivable	1,424	(4,862)
Other receivables	(508)	638
Inventories	(2,161)	(72)
Prepaid expenses and other assets	2	(951)
Accounts payable	47	(1,231)
Accrued and other liabilities	(3,121)	1,102
Deferred revenue	1,715	3,004
Net cash (used in) provided by operating activities	(3,320)	5,814
Cash flows from investing activities		
Purchase of property and equipment	(3,484)	(1,379)
Purchase of short-term investments	(113,199)	(87,383)
Maturities of short-term investments	41,290	13,986
Net cash used in investing activities	(75,393)	(74,776)
Cash flows from financing activities		
Cash from lease-related performance obligations	743	713
Principal payments on long-term borrowings	—	(8,333)
Proceeds from initial public offering, net of offering costs	—	72,217
Proceeds from follow-on public offering, net of offering costs	—	35,996
Payment for repurchase of early exercised options	(14)	(6)
Excess tax benefits from employee stock plans	—	300
Proceeds from issuance of common stock from the employee stock purchase plan	2,572	—
Proceeds from exercise of stock options	1,426	863
Tax withholdings paid on behalf of employees for net share settlement	(476)	—
Proceeds from exercise of common stock warrants	226	—
Net cash provided by financing activities	4,477	101,750
Net (decrease) increase in cash and cash equivalents	(74,236)	32,788
Cash and cash equivalents at beginning of period	92,521	14,898
Cash and cash equivalents at end of period	$18,285	$47,686

Supplemental disclosure of non-cash investing and financing activities:		
Costs related to the initial public offering in accounts payable and accrued liabilities	$—	$190
Property and equipment in accounts payable and accrued liabilities	112	—

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

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Notes to Unaudited Condensed Consolidated Financial Statements

1. The Company and Summary of Significant Accounting Policies

Vocera Communications, Inc. ("Vocera" or the "Company") is a provider of mobile communication solutions focused on addressing the challenges facing hospitals, as well as hospitality, power and other businesses with mission-critical communication needs, in the U.S. and internationally. Vocera helps its healthcare customers improve patient safety and satisfaction, and increase hospital efficiency and productivity through its Voice Communication, Secure Messaging, and Care Experience solutions, which are installed in more than 1,000 organizations worldwide. The Voice Communication solution, which includes a lightweight, wearable, voice-controlled communication badge, smartphone applications and an intelligent enterprise software platform, enables users to connect instantly with other staff simply by saying the name, function or group name of the desired recipient. The Secure Messaging solution securely delivers text messages and alerts directly to and from smartphones, replacing legacy pagers. Our Vocera Care Experience is a hosted, software solution suite that coordinates and streamlines patient-to-provider and provider-to-provider communication across the continuum of care. The solution is used to provide personalized patient instructions and education, alert and notify physicians and caregivers of patients' changing care plans, and track patient satisfaction pre, during, and post-hospitalization. Vocera Care Experience is complemented by the Company's Experience Innovation Network, a membership-based program to spread the adoption of leading strategies to improve patient and staff experience.

The Company was incorporated in Delaware on February 16, 2000. The Company formed wholly-owned subsidiaries Vocera Communications UK Ltd and Vocera Communications Australia Pty Ltd. in 2005, and Vocera Hand-Off Communications, Inc., Vocera Canada, Ltd. and ExperiaHealth, Inc. in 2010. In August 2013, we merged Vocera Hand-Off Communications, Inc. and ExperiaHealth, Inc. into our parent company, Vocera Communications, Inc.

The Company completed its initial public offering ("IPO") of common stock on April 2, 2012 in accordance with the Securities Act of 1933, as amended ("Securities Act"). The Company sold 5,000,000 shares and certain of its stockholders sold 1,727,500 shares, including 877,500 shares for the underwriters' over-allotment option, through a firm commitment underwritten, public offering. The shares were sold at the initial public offering price of $16.00 per share, before underwriting discounts and commissions and offering costs. The Company recorded proceeds of $70.5 million for the IPO, net of offering expenses and underwriters' discounts and commissions.

The Company completed a follow-on offering of common stock on September 12, 2012 in accordance with the Securities Act. The Company sold 1,337,500 shares and certain of its stockholders sold 4,211,250 shares. Included in both of these sales was 723,750 shares for the underwriters' over-allotment option, through a firm commitment underwritten, public offering. The shares were sold at the public offering price of $28.75 per share for aggregate gross offering proceeds of $38.4 million to the Company and $121.1 million to the selling stockholders. The Company recorded proceeds of $36.0 million for the follow-on offering, net of offering expenses and underwriters' discounts and commissions.

Basis of presentation

The Company's unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X of the U.S. Securities and Exchange Commission, and include the accounts of Vocera and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated. Certain information and note disclosures normally included in the financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. Accordingly, these unaudited interim condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2012. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly the Company's interim consolidated financial information. The results for the quarter presented are not necessarily indicative of the results to

be expected for the year ending December 31, 2013 or for any other interim period or any other future year.
Use of Estimates
The preparation of the accompanying unaudited condensed consolidated financial statements in conformity with U.S. GAAP requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting periods. The estimates include, but are not limited to, revenue recognition, useful lives assigned to

long-lived assets, excess and obsolete inventory charges, warranty reserves, stock-based compensation expense, provisions for income taxes and contingencies. Actual results could differ from these estimates, and such differences could be material to the Company's financial position and results of operations.

Fair Value of Financial Instruments

The carrying value of the Company's operating financial instruments, including accounts receivable, deposits, accounts payable, accrued liabilities and accrued compensation, approximates fair value due to their short maturities. Cash and cash equivalents and short-term investments are carried at fair value.

Cash Equivalents and Short-term Investments

The Company's cash equivalents and short-term investments consist of money market funds, commercial paper, U.S. government agency notes, U.S. Treasury notes, municipal debt and corporate debt. These investments are classified as available-for-sale securities and are carried at fair value with the unrealized gains and losses reported as a component of stockholders' equity. Management determines the appropriate classification of its investments at the time of purchase and re-evaluates the available-for-sale designations as of each balance sheet date. Investments with an original purchase maturity of less than three months are classified as cash equivalents, all those with longer maturities are classified as short-term investments.

Deferred Costs of Revenue

When the Company's products have been delivered, but the product revenue associated with the arrangement has been deferred as a result of not meeting the revenue recognition criteria, the Company also defers the related inventory costs for the delivered items. The Company includes such deferred cost of revenue as part of "Prepaid expenses and other current assets" in the accompanying condensed, consolidated balance sheet.

Revenue recognition

The Company derives revenue from the sales of communication badges, smartphone application software, perpetual software licenses for enterprise software that is essential to the functionality of the communication badges, software maintenance, extended warranty and professional services. The Company also derives revenue from the sale of licenses for software that is not essential to the functionality of the communication badges. The Company's revenue recognition policy has not changed from that described in its Annual Report on Form 10-K for the year ended December 31, 2012.

A portion of the Company's sales are made through multi-year lease agreements with customers. When these arrangements are considered sales-type leases, upon delivery of leased products to customers, the Company recognizes revenue for such products in an amount equal to the net present value of the minimum lease payments. Unearned income is recognized as part of product revenue under the effective interest method. The Company recognizes revenue related to executory costs when such executory costs are incurred.

Proceeds from transfers of sales-type leases to third-party financial companies are allocated between the net investment in sales-type leases and the executory cost component for remaining service obligations based on relative present value. The difference between the amount of proceeds allocated to the net investment in lease and the carrying value of the net investment in lease is included in product revenue. Proceeds allocated to the executory cost component are accounted for as financing liabilities.

For the three months and nine months ended September 30, 2013, the Company transferred $0.2 million and $1.0 million, respectively, of lease receivables with immaterial net gains in each period. For the three months and nine months ended September 30, 2013, the Company recorded $0.2 million and $0.7 million, respectively, of financing liabilities for future performance of executory service obligations. For lease receivables retained as of September 30, 2013, the Company recorded $1.1 million of net investment in sales-type leases, equivalent to the minimum lease payments less the unearned interest portion.

Related party transactions

During the nine months ended September 30, 2013 the Company billed a related party, the University of Chicago Medical Center ("UCMC"), $0.5 million for consulting services. One of the Company's board members, Sharon O'Keefe is also on the board of the UCMC. These transactions were recorded at arms-length prices.

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Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board ("FASB") issued new disclosure guidance related to the presentation of the statement of comprehensive income. This guidance eliminated the previous option to report other comprehensive income (“OCI”) and its components in the consolidated statement of stockholders' equity. The Company adopted this accounting standard effective January 1, 2012; the adoption had no material impact on the financial position or results of operations of the Company. In February 2013, the FASB resolved the deferred guidance on OCI reclassifications with a new rule effective in the first quarter of 2013, which was adopted but did not have a material impact.

In July 2013, the FASB issued new guidance for the gross versus net presentation of unrecognized tax benefits. The FASB concluded that an unrecognized tax benefit should be presented as a reduction of a deferred tax asset for a net operating loss (“NOL”) or other tax credit carryforward when settlement in this manner is available under the tax law. The new guidance is effective for the Company's first quarter of 2014, applied prospectively. The Company has the option to apply the rule retrospectively and early adoption is permitted. Adoption of this standard is not expected to impact the financial position or results of operations of the Company.

2. Fair value of financial instruments

The Company’s cash and cash equivalents and short-term investments are carried at their fair values with any differences from their amortized cost recorded in equity as unrealized gains (losses) on marketable securities. As a basis for determining the fair value of its assets and liabilities, the Company established a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows: (Level 1) observable inputs such as quoted prices in active markets; (Level 2) inputs other than the quoted prices in active markets that are observable either directly or indirectly; and (Level 3) unobservable inputs in which there is little or no market data which requires the Company to develop its own assumptions. This hierarchy requires the Company to use observable market data, when available, and to minimize the use of unobservable inputs when determining fair value. For the nine months ended September 30, 2013 there have been no transfers between Level 1 and Level 2 fair value instruments and no transfers in or out of Level 3.

The Company's money market funds are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices. The fair value of the Company's Level 2 fixed income securities are obtained from independent pricing services, which may use quoted market prices for identical or comparable instruments or model-driven valuations using observable market data or other inputs corroborated by observable market data.

The Company’s assets that are measured at fair value on a recurring basis, by level, within the fair value hierarchy as of September 30, 2013 and December 31, 2012, are summarized as follows (in thousands):

	September 30, 2013			December 31, 2012		
	Level 1	Level 2	Total	Level 1	Level 2	Total
Assets						
Money market funds	$989	$—	$989	$45,040	$—	$45,040
Commercial paper	—	4,134	4,134	—	32,487	32,487
U.S. government agency securities	—	11,514	11,514	—	10,001	10,001
U.S. Treasury securities	—	5,257	5,257	—	—	—
Municipal debt securities	—	4,785	4,785	—	—	—
Corporate debt securities	—	85,447	85,447	—	—	—
Total assets measured at fair value	$989	$111,137	$112,126	$45,040	$42,488	$87,528

The Company had no liabilities as of September 30, 2013 and December 31, 2012 that were measured at fair value on a recurring basis.

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3. Cash, Cash Equivalents and Short-Term Investments

The following tables present current and prior-year-end balances for cash, cash equivalents and short-term investments (in thousands):

	As of September 30, 2013			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair value
Cash and cash equivalents:				
Demand deposits and other cash	$13,106	$—	$—	$13,106
Money market funds	989	—	—	989
Commercial paper	2,000	—	—	2,000
Corporate debt securities	2,190	—	—	2,190
Total cash and cash equivalents	18,285	—	—	18,285
Short-Term Investments:				
Commercial paper	2,134	—	—	2,134
U.S. government agency securities	11,511	5	(2)	11,514
U.S. Treasury securities	5,254	3	—	5,257
Municipal debt securities	4,781	4	—	4,785
Corporate debt securities	83,265	11	(19)	83,257
Total short-term investments	106,945	23	(21)	106,947
Total cash, cash equivalents and short-term investments	$125,230	$23	$(21)	$125,232

The company has determined that the unrealized losses on cash equivalents and short-term investments as of September 30, 2013 do not constitute an "other than temporary impairment."

	As of December 31, 2012			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair value
Cash and cash equivalents:				
Demand deposits and other cash	$39,982	$—	$—	$39,982
Money market funds	45,040	—	—	45,040
Commercial paper	7,498	1	—	7,499
Total cash and cash equivalents	92,520	1	—	92,521
Short-Term Investments:				
Commercial paper	24,987	1	—	24,988
U.S. government agency securities	9,998	3	—	10,001
Total short-term investments	34,985	4	—	