VOCERA COMMUNICATIONS, INC.
Form 10-Q
May 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 March 31, 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 May 2, 2013

Common Stock, $0.0003 par value per share	24,501,724 shares

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VOCERA COMMUNICATIONS, INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 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)

	March 31, 2013	December 31, 2012
Assets		
Current assets		
Cash and cash equivalents	$116,407	$92,521
Short-term investments	10,000	34,989
Accounts receivable, net of allowance of $23 and $0 at March 31, 2013 and December 31, 2012, respectively	14,886	21,697
Other receivables	333	550
Inventories	4,565	2,772
Prepaid expenses and other current assets	3,719	2,808
Total current assets	149,910	155,337
Property and equipment, net	4,713	3,631
Intangible assets, net	2,087	2,267
Goodwill	5,575	5,575
Other long-term assets	515	495
Total assets	$162,800	$167,305
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$3,021	$2,854
Accrued payroll and other liabilities	7,572	11,754
Deferred revenue, current	21,748	22,451
Total current liabilities	32,341	37,059
Deferred revenue, long-term	5,410	5,882
Other long-term liabilities	1,269	1,239
Total liabilities	39,020	44,180
Commitments and contingencies (Note 7)		
Stockholders' equity		
Preferred stock, $0.0003 par value - 5,000,000 shares authorized as of March 31, 2013 and December 31, 2012; zero shares issued and outstanding	—	—
Common stock, $0.0003 par value - 100,000,000 shares authorized as of March 31, 2013 and December 31, 2012; 24,481,612 and 24,229,356 shares issued and outstanding as of March 31, 2013 and December 31, 2012, respectively	7	7
Additional paid-in capital	181,239	177,081
Accumulated other comprehensive income	1	5
Accumulated deficit	(57,467)	(53,968)
Total stockholders’ equity	123,780	123,125
Total liabilities and stockholders’ equity	$162,800	$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 March 31,	
	2013	2012
Revenue		
Product	$12,960	$14,637
Service	9,453	8,482
Total revenue	22,413	23,119
Cost of revenue		
Product	4,610	5,429
Service	4,084	3,569
Total cost of revenue	8,694	8,998
Gross profit	13,719	14,121
Operating expenses		
Research and development	3,614	2,511
Sales and marketing	10,232	7,530
General and administrative	3,298	3,087
Total operating expenses	17,144	13,128
(Loss) income from operations	(3,425)	993
Interest income	24	12
Interest expense and other finance charges	—	(71)
Other expense, net	(47)	(1,597)
Loss before income taxes	(3,448)	(663)
Provision for income taxes	(51)	(173)
Net loss	$(3,499)	$(836)
Net loss per share attributable to common stockholders		
Basic and diluted	$(0.14)	$(0.23)
Weighted average shares used to compute net loss per share attributable to common stockholders		
Basic and diluted	24,282	3,661

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 Loss
(In Thousands)
(Unaudited)

	Three months ended March 31,	
	2013	2012
Net loss	$(3,499)	$(836)
Other comprehensive loss, net:		
Decrease in unrealized gain on investments, net	(4)	—
Comprehensive loss	$(3,503)	$(836)

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)

	Three months ended March 31,	
	2013	2012
Cash flows from operating activities		
Net loss	$(3,499)	$(836)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	536	553
Change in non-cash interest	14	—
Loss on disposal of property and equipment	—	3
Allowance for doubtful accounts	23	—
Inventory write-down	26	4
Stock-based compensation expense	1,704	317
Non-employee stock-based compensation expense	—	29
Excess tax benefits from employee stock plans - operating	(257)	—
Change in fair value of warrant liability	—	1,706
Changes in operating assets and liabilities:		
Accounts receivable	6,789	(45)
Other receivables	115	(161)
Inventories	(1,819)	264
Prepaid expenses and other assets	(932)	(747)
Accounts payable	133	(1,942)
Accrued and other liabilities	(3,844)	94
Deferred revenue	(1,175)	1,029
Net cash (used in) provided by operating activities	(2,186)	268
Cash flows from investing activities		
Purchase of property and equipment	(1,502)	(545)
Maturities of short-term investments	24,971	—
Net cash provided by (used in) investing activities	23,469	(545)
Cash flows from financing activities		
Cash from lease-related performance obligations	106	—
Principal payments on long-term borrowings	—	(500)
Payment for repurchase of early exercised options	(3)	(6)
Excess tax benefits from employee stock plans - financing	257	—
Proceeds from issuance of common stock from the employee stock purchase plan	1,596	—
Proceeds from exercise of stock options	421	288
Proceeds from exercise of common stock warrants	226	—
Common stock issuance costs	—	(250)
Net cash provided by (used in) financing activities	2,603	(468)
Net increase (decrease) in cash and cash equivalents	23,886	(745)
Cash and cash equivalents at beginning of period	92,521	14,898
Cash and cash equivalents at end of period	$116,407	$14,153
Supplemental disclosure of non-cash investing and financing activities:		
	$—	$1,988

Costs related to the initial public offering in accounts payable and accrued liabilities		
Property and equipment in accounts payable and accrued liabilities	257	116

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 critical communication challenges facing hospitals today. Vocera helps its customers improve patient safety and satisfaction, and increase hospital efficiency and productivity through its Voice Communication, Secure Messaging, and Care Transition solutions. The Voice Communication solution, which includes a lightweight, wearable, voice-controlled communication badge and a software platform, enables users to connect instantly with other hospital 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. The Care Transition solution is a hosted voice and text based software application that captures, manages and monitors patient information when responsibility for the patient is transferred or “handed-off” from one caregiver to another, or when the patient is discharged from the hospital. These three solutions are complemented by the Company's ExperiaHealth business, which is focused on improving patient 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, Inc., Vocera Canada, Ltd. and ExperiaHealth, Inc. in 2010.

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. Certain prior period amounts have been reclassified to be consistent with current period presentation.

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, 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.

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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 and U.S. agency notes. 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 reevaluates 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, those with longer maturities are classified as short-term investments. As of March 31, 2013 and December 31, 2012, all of the Company's available-for-sale securities had maturities of less than one year.

Revenue recognition

The Company derives revenue from the sales of communication badges, smartphones, perpetual software licenses for 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 ended March 31, 2013, the Company transferred $0.3 million of lease receivables and recorded $0.1 million of financing liabilities for future performance of executory service obligations. For lease receivables retained as of March 31, 2013, the Company recorded $0.1 million of net investment in sales-type leases, equivalent to the minimum lease payments less the unearned interest portion.

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, or 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 any material impact.

2. Fair value of financial instruments

The Company’s cash and cash equivalents and short-term investments are carried at their fair values, usually with immaterial differences from their amortized cost, due to their short-term nature. 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 three months ended March 31, 2013 there have been no transfers between Level 1 and Level 2 fair value instruments and no transfers in or out of Level 3.

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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 Company's other cash equivalents and short-term investments are classified within Level 2 of the fair value hierarchy because they are valued by professional pricing services using market-corroborated inputs from similar instruments, rather than direct observation of quoted prices in active markets. Each security is compared to a benchmark yield at the balance sheet date, with adjustment for its specific characteristics.

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

	March 31, 2013				December 31, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Money market funds	$77,542	$—	$—	$77,542	$45,040	$—	$—	$45,040
Commercial paper	—	—	—	—	—	32,487	—	32,487
U.S. government and agency securities	—	10,000	—	10,000	—	10,001	—	10,001
Total assets measured at fair value	$77,542	$10,000	$—	$87,542	$45,040	$42,488	$—	$87,528

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

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 March 31, 2013			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair value
Cash and cash equivalents:				
Demand deposits and other cash	$38,865	$—	$—	$38,865
Money market funds	77,542	—	—	77,542
Total cash and cash equivalents	116,407	—	—	116,407
Short-Term Investments:				
U.S. government and agency securities	9,999	1	—	10,000
Total short-term investments	9,999	1	—	10,000
Total cash, cash equivalents and short-term investments	$126,406	$1	$—	$126,407

	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 and agency securities	9,998	3	—	10,001
Total short-term investments	34,985	4	—	34,989
Total cash, cash equivalents and short-term investments	$127,505	$5	$—	$127,510

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The tables above exclude restricted cash, primarily held in certificates of deposit, of $0.3 million as of March 31, 2013 and December 31, 2012 which are classified in prepaids and other current assets on the balance sheet.

4. Income (loss) per share

Basic and diluted net loss per common share is presented in conformity with the two-class method required for participating securities. Immediately prior to the completion of the Company's IPO in April 2012, holders of Series A through Series F convertible preferred stock were each entitled to receive non-cumulative dividends at the annual rate of 8% per share per annum, respectively, payable prior and in preference to any dividends on any shares of the Company's common stock. In the event a dividend were to be paid on common stock, the holders of convertible preferred stock were entitled to a proportionate share of any such dividend as if they were holders of common stock (on an as-if converted basis). The holders of the convertible preferred stock did not have a contractual obligation to share the losses of the Company. The Company considered its convertible preferred stock as participating securities. Additionally, the Company considers shares issued upon the early exercise of options subject to repurchase and unvested restricted shares to be participating securities as the holders of these shares have a non-forfeitable right to dividends. In accordance with the two-class method, earnings allocated to these participating securities and the related number of outstanding shares of the participating securities, which include contractual participation rights in undistributed earnings, have been excluded from the computation of basic and diluted net loss per common share. Under the two-class method, net income (loss) attributable to common stockholders is determined by allocating undistributed earnings, calculated as net income less income attributable to participating securities between common stock and participating securities. In computing net income (loss) attributable to common stockholders for calculation of diluted net income (loss) per share, undistributed earnings are re-allocated to reflect the potential impact of dilutive securities. Basic net income (loss) per common share is computed by dividing the net income (loss) attributable to common stockholders by the weighted-average number of common shares outstanding during the period. All participating securities are excluded from basic weighted-average common shares outstanding. Diluted net income (loss) per share attributable to common stockholders is computed by dividing the net income (loss) attributable to common stockholders for calculation of diluted net income (loss) per share by the weighted-average number of common shares outstanding, including potential dilutive common shares assuming the dilutive effect of outstanding stock options using the treasury stock method.

The following table sets forth the computation of basic and diluted net loss per share (in thousands, except per share amounts):

	Three months ended March 31,	
	2013	2012
Numerator:		
Net loss	$(3,499)	$(836)
Denominator:		
Weighted-average shares used to compute net loss per common share- basic and diluted	24,282	3,661
Net loss per share		
Net loss per common share - basic and diluted	$(0.14)	$(0.23)

The following securities were not included in the calculation of diluted shares outstanding as the effect would have been anti-dilutive:

	Three months ended March 31,	
(in thousands)	2013	2012
Convertible preferred stock (on an if converted basis)	—	12,938
Options to purchase common stock	3,180	3,682
Common stock subject to repurchase	36	195
Warrants to purchase convertible preferred stock	—	187
Warrants to purchase common stock	44	—

Restricted stock units	441	—
Restricted stock awards	12	—

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5. Goodwill and intangible assets

Goodwill

As of March 31, 2013 and December 31, 2012, the Company had $5.6 million of goodwill acquired. Goodwill is tested for impairment at the reporting unit level at least annually or more often if events or changes in circumstances indicate the carrying value may not be recoverable. The Company performed the annual required test of impairment of goodwill as of September 30, 2012, using the qualitative approach (or "Step Zero") as permitted by FASB's rules for goodwill impairment testing. The Company’s annual impairment test did not indicate impairment at any of its reporting units. No impairment was recorded in 2012. As of March 31, 2013, no changes in circumstances indicate that goodwill carrying values may not be recoverable.

Intangible assets

The fair values for acquired intangible assets were determined by management using the valuations performed by independent valuation specialists. Acquisition related intangible assets are amortized over the life of the assets on a basis that resembles the economic benefit of the assets. This results in amortization that is higher in earlier periods of the useful life. The estimated useful lives and carrying value of acquired intangible assets are as follows:

		March 31, 2013			December 31, 2012		
(in thousands)	Weighted Average Useful Life (years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	9	$2,350	$1,201	$1,149	$2,350	$1,117	$1,233
Developed technology	6	1,880	988	892	1,880	896	984
Trademarks	7	70	33	37	70	30	40
Non-compete agreements	2	70	61	9	70	60	10
Intangible assets		$4,370	$2,283	$2,087	$4,370	$2,103	$2,267

Amortization expense was $0.2 million and $0.2 million for the three months ended March 31, 2013 and March 31, 2012, respectively.

Amortization of acquired intangible assets is reflected in cost of revenue and operating expenses. The estimated future amortization of existing acquired intangible assets as of March 31, 2013 was as follows (in thousands):

(in thousands)	Future amortization
2013 (remaining nine months)	$547
2014	567
2015	389
2016	258
2017	156
Thereafter	170
Future amortization expense	$2,087

6. Balance Sheet Components

Inventories

(in thousands)	March 31, 2013	December 31, 2012
Raw materials	$815	$23
Finished goods	3,750	2,749
Total inventories	$4,565	$2,772

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Property and Equipment

(in thousands)	March 31, 2013	December 31, 2012
Computer equipment and software	$4,281	$4,127
Furniture, fixtures and equipment	886	886
Leasehold improvements	1,663	1,654
Manufacturing tools and equipment	2,784	2,710
Construction in process	2,301	1,100
Property and equipment, at cost	11,915	10,477
Less: Accumulated depreciation	(7,202)	(6,846)
Property and equipment, net	$4,713	$3,631

Depreciation and amortization expense was $0.4 million and $0.3 million for the three months ended March 31, 2013 and March 31, 2012, respectively.

Accrued payroll and other liabilities

(in thousands)	March 31, 2013	December 31, 2012
Payroll and related expenses	$3,925	$7,845
Accrued payables	1,551	1,823
Deferred rent, current portion	610	591
Lease financing, current portion	302	213
Product warranty	207	297
Exercise of unvested stock options	160	198
Customer prepayments	188	115
Sales and use tax payable	348	323
Other	281	349
Total accrued payroll and other liabilities	$7,572	$11,754

The Company generally provides for the estimated costs of product warranties at the time the related revenue is recognized. Costs are estimated based on historical and projected product failure rates, historical and projected repair or replacement costs, and knowledge of specific product failures (if any). The product warranty includes parts and labor over a period of one year. The Company provides no warranty for software. The Company regularly re-evaluates its estimates to assess the adequacy of the recorded warranty liabilities and to adjust the amounts as necessary.

The changes in the Company's product warranty reserve are as follows:

	Three months ended March 31,	
(in thousands)	2013	2012
Balance at the beginning of the period	$297	$983
Warranty expense accrued for shipments in period	74	354
Changes in liability related to pre-existing warranties	49	149
Warranty settlements made	(213)	(257)
Balance at the end of the period	$207	$1,229

7. Commitments and contingencies

The Company undertakes, in the ordinary course of business, to (i) defend customers and other parties from certain third-party claims associated with allegations of trade secret misappropriation, infringement of copyright, patent or other intellectual property right, or tortious damage to persons or property and (ii) indemnify and hold harmless such parties from certain resulting damages, costs and other liabilities. The term of these undertakings may be perpetual and the maximum potential liability of the Company under certain of these undertakings is not determinable. The Company has never incurred costs to

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defend lawsuits or settle claims related to these undertakings and, as a result, the Company believes the corresponding estimated fair value is minimal.

The Company has entered into indemnification agreements with its directors and officers that may require the Company to indemnify its directors and officers against liabilities that may arise by reason of their status or service as directors or officers, other than liabilities arising from willful misconduct of the individual. The Company currently has directors and officers insurance.

Non-cancelable purchase commitments

The Company enters into non-cancelable purchase commitments with its third-party manufacturer whereby the Company is required to purchase any inventory held by the third party manufacturer that have been purchased by them based on confirmed orders from the Company. As of March 31, 2013 and December 31, 2012, approximately $4.1 million and $4.1 million, respectively, of raw material inventory was purchased and held by the third-party manufacturer which was subject to such purchase requirements.

Leases

The Company leases office space for its headquarters and subsidiaries under non-cancelable operating leases, which will expire between April 2014 and April 2017. The Company recognizes rent expense on a straight-line basis over the lease period, and has accrued for rent expense incurred but not paid.

Future minimum lease payments at March 31, 2013 under non-cancelable operating leases are as follows (in thousands):

(in thousands)	Operating leases
2013 (remaining nine months)	$1,194
2014	1,545
2015	1,480
2016	440
2017 and thereafter	30
Total minimum lease payments	$4,689

8. Stock-based Compensation and Awards

Equity Incentive Plans

The Company has three equity incentive plans: the 2000 Stock Option Plan (the "2000 Plan"), the 2006 Stock Option Plan (the "2006 Plan") and the 2012 Stock Option Plan (the "2012 Plan"). On March 26, 2012, all shares that were reserved under the 2006 Plan but not subject to outstanding awards became available for grant under the 2012 Plan. No additional shares will be issued under the 2006 Plan. The 2000 Plan terminated in March 2010 and no additional shares will be issued under this plan. All options currently outstanding under the 2000 Plan and the 2006 Plan continue to be governed by the terms and conditions of those plans. Under the 2012 Plan, the Company has the ability to issue incentive stock options (“ISOs”), stock appreciation rights, restricted stock, restricted stock units (“RSUs”), performance awards and stock bonuses. The ISOs will be granted at a price per share not less than the fair value at date of grant. Options granted to date generally vest over a four-year period with 25% vesting at the end of one year and the remaining vest monthly thereafter. Options granted generally are exercisable up to 10 years.

Early Exercise of Stock Options

The Company typically allows employees to exercise options granted under the 2000 and 2006 Plans prior to vesting. The unvested shares are subject to the Company’s repurchase right at the original purchase price. The proceeds initially are recorded as an accrued liability from the early exercise of stock options (see Note 6, Accrued Liabilities), and reclassified to common stock as the Company’s repurchase right lapses. As of March 31, 2013 and December 31, 2012, 35,585 and 48,260 shares held by employees were subject to repurchase at an aggregate price of $0.2 million and $0.2 million, respectively.

Cash exercise of common stock warrants

During the three months ended March 31, 2013 holders of common stock warrants exercised 34,142 shares for cash proceeds of $0.2 million. There were no cash exercises in the prior year period.

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Stock Option Activity

A summary of the stock option activity for the three months ended March 31, 2013 is presented below:

	Options outstanding				
	Shares Available for Grant	Number of Options	Weighted Average Exercise Price	Weighted average remaining contractual term (in years)	Aggregate intrinsic value (in thousands)
Outstanding at December 31, 2012	460,579	3,187,559	$7.51	6.8	$56,362
Shares added to the plan	1,211,487				
Options granted	(108,145)	108,145	25.98		
Options exercised	—	(103,822)	3.07		
Options canceled	11,529	(11,529)	11.94		
Options expired	229	(229)	11.10		
Early exercised options repurchased and added back to the pool	1,492	—			
Outstanding at March 31, 2013	1,577,171	3,180,124	$8.26	6.7	$48,104

The cash received for exercises of stock options during the three months ended March 31, 2013 includes the collection of approximately $0.1 million classified in other receivables at December 31, 2012.

At March 31, 2013, there was $7.7 million of unrecognized net compensation cost related to options which is expected to be recognized over a weighted-average period of 2.6 years. The Company did not grant non-employee options in either of the three months ended March 31, 2013 or 2012.

The Company uses the Black-Scholes option-pricing model to calculate the fair value of stock options on their grant date. This model requires the following inputs: the estimated fair value of the underlying common stock, the expected term of the option, the expected volatility of the underlying common stock over the expected life of the option, the risk-free interest rate and expected dividend yield.

The following assumptions were used for each respective period for employee stock options:

	Three months ended March 31,	
	2013	2012
Expected Term (in years)	5.43	5.60
Volatility	48.1%	47.9%
Risk-free interest rate	0.81%	1.03%
Dividend yield	0%	0%

Employee Stock Purchase Plan

In March 2012, the Company’s 2012 Employee Stock Purchase Plan (the “ESPP”) was approved. The ESPP allows eligible employees to purchase shares of the Company’s common stock at a discount through payroll deductions of up to 15% of their eligible compensation, subject to any plan limitations. The ESPP generally provides for six-month offering periods, except for the first offering period which was for eleven months. Additionally, in April 2013, our compensation committee determined the next offering period under our ESPP, which will commence on August 15, 2013, will last for a duration of three months (expiring on November 14, 2013) and, following the expiration of such offering period, each offering period thereafter will commence on each November 15 and May 15 and will have of a single six month purchase period.

At the end of each offering period, employees are able to purchase shares at 85% of the lower of the fair market value of the Company’s common stock on the first trading day of the offering period or on the last day of the offering period. On the initial purchase date during the three months ended March 31, 2013, employees purchased 115,784 shares of common stock at an average exercise price of $13.79. As of March 31, 2013, there were 293,175 shares which remained available for future issuance under the ESPP.

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The following assumptions were used for each respective period for the ESPP:

	Three months ended March 31,	
	2013	2012
Expected Term (in years)	0.50	0.88
Volatility	33.3%	50.8%
Risk-free interest rate	0.13%	0.18%
Dividend yield	0%	0%

Restricted Stock Awards and Restricted Stock Units

In 2012, the Company began incorporating restricted stock awards and RSUs as an element of the Company's compensation plans. In February 2012, the Company granted certain of its directors restricted stock which vests 50% on the first anniversary of the grant and 50% on the second anniversary of the grant. Since May 2012, the Company has granted certain employees RSUs, which vest one-third on the first anniversary of the grant date, one-third on the second anniversary of the grant date and one-third upon the third anniversary of the grant date.

A summary of restricted stock activity for the three months ended March 31, 2013 is presented below:

	Restricted Stock Awards		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
Outstanding at December 31, 2012	24,152	$12.42	373,908	$25.34
Granted	—	—	78,149	25.99
Vested	(12,076)	12.42	—	—
Forfeited	—	—	(10,939)	25.37
Outstanding at March 31, 2013	12,076	$12.42	441,118	$25.41

At March 31, 2013, there was $0.1 million of unrecognized net compensation cost related to restricted stock awards which is expected to be recognized over a weighted-average period of 0.9 years. At March 31, 2013, there was $8.5 million of unrecognized net compensation cost related to RSUs which is expected to be recognized over a weighted-average period of 2.4 years.

Allocation of Stock-Based Compensation Expense

Stock-based compensation expense is recognized based on a straight-line amortization method over the respective vesting period of the award and has been reduced for estimated forfeitures. The Company estimated the expected forfeiture rate based on its historical experience, considering voluntary termination behaviors, trends of actual award forfeitures, and other events that will impact the forfeiture rate. To the extent the Company's actual forfeiture rate is different from the estimate, the stock-based compensation expense is adjusted accordingly.

The following table presents the stock-based compensation allocation of expense (both for employees and non-employees):

	Three months ended March 31,	
(in thousands)	2013	2012
Cost of revenue	$222	$21
Research and development	209	26
Sales and marketing	579	66
General and administrative	694	233
Total stock based compensation	$1,704	$346

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9. Segments

The Company has two operating segments which are both reportable business segments: (i) Product and (ii) Service, both of which are comprised of Vocera's and its wholly-owned subsidiaries' results from operations. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker (CODM), or decision making group, in deciding how to allocate resources and in assessing performance. The Company's CODM is its Chief Executive Officer.

The CODM regularly receives information related to revenue, cost of revenue, and gross profit for each operating segment, and uses this information to assess performance and make resource allocation decisions. All other financial information, including operating expenses and assets, is prepared and reviewed by the CODM on a consolidated basis. Assets are not a measure used to assess the performance of the Company by the CODM; therefore, the Company does not report assets by segment internally or in its financial statements.

The following table presents a summary of the operating segments:

	Three months ended March 31,	
(in thousands)	2013	2012
Revenue		
Product	$12,960	$14,637
Service	9,453	8,482
Total revenue	22,413	23,119
Cost of Revenue		
Product	4,610	5,429
Service	4,084	3,569
Total cost of revenue	8,694	8,998
Gross profit		
Product	8,350	9,208
Service	5,369	4,913
Total gross profit	13,719	14,121
Operating expenses	17,144	13,128
Interest income (expense), net and other	(23)	(1,656)
Loss before income taxes	$(3,448)	$(663)

10. Income Taxes

Income tax expense was $51,000 and $173,000 for the three months ended March 31, 2013 and 2012, respectively. The positive tax expense in both periods was primarily due to profitable international operations and, for the three months ended March 31, 2012, profitable international operations and state income taxes.

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the carrying amounts of existing assets and liabilities in the financial statements and their respective tax bases using tax rates expected to be in effect during the years in which the basis differences reverse.

The Company determines its valuation allowance on deferred tax assets by considering both positive and negative evidence in order to ascertain whether it is more likely than not that deferred tax assets will be realized. Realization of deferred tax assets is dependent upon the generation of future taxable income, if any, the timing and amount of which are uncertain. Due to the history of losses the Company has generated in past years and the $3.5 million net loss for the three months ended March 31, 2013, the Company believes that it is not more likely than not that its deferred tax assets can be realized as of March 31, 2013. Accordingly, the Company has retained the full valuation allowance on its deferred tax assets previously determined for the year ended December 31, 2012.

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While the Company generated pretax profit in 2012, management believes it is appropriate to obtain confirmatory evidence that the Company's results of operations will sustain this profitability in 2013, before reversing a portion of the valuation allowance to earnings.

The Company will review on a quarterly basis its conclusions about the appropriate amount of its deferred income tax asset valuation allowance. If the Company generates profits in 2013, it is likely that the US valuation allowance position may be reversed in the foreseeable future. The Company expects a significant benefit in the period the valuation allowance reversal is recorded and a significantly higher effective tax rate in periods following the valuation allowance reversal.

As of March 31, 2013, there were no material changes to either the nature or the amounts of the uncertain tax positions previously determined for the year ended December 31, 2012.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and the related notes that appear elsewhere in this Form 10-Q. These discussions contain forward-looking statements reflecting our current expectations that involve risks and uncertainties which are subject to safe harbors under the Securities Act of 1933, as amended, or the Securities Act, and the Securities Exchange Act of 1934, as amended, or the Exchange Act. These forward-looking statements include, but are not limited to, statements concerning our plans, objectives, expectations and intentions, future financial position, future revenues, projected costs, expectations regarding demand and acceptance for our technologies, growth opportunities and trends in the market in which we operate, prospects and plans and objectives of management. The words “anticipates,” “believes,” “estimates," “expects,” “intends,” “may,” “plans,” “projects,” “will,” “would” and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements, and you should not place undue reliance on our forward-looking statements. These forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those in the forward-looking statements, including, without limitation, the risks set forth in Part II, Item 1A, “Risk Factors” in this Quarterly Report on Form 10-Q and in our other filings with the Securities and Exchange Commission. We do not assume any obligation to update any forward-looking statements.

Business overview

We are a provider of mobile communication solutions focused on addressing critical communication challenges facing hospitals today. We help our customers improve patient safety and satisfaction, and increase hospital efficiency and productivity through our Voice Communication, Secure Messaging and Care Transition solutions. Our Voice Communication solution, which includes a lightweight, wearable, voice-controlled communication badge and a software platform, enables users to connect instantly with other hospital staff simply by saying the name, function or group name of the desired recipient. Our Secure Messaging solution securely delivers text messages and alerts directly to and from smartphones, replacing legacy pagers. Our Care Transition solution is a hosted voice and text based software application that captures, manages and monitors patient information when responsibility for the patient is transferred or “handed-off” from one caregiver to another, or when the patient is discharged from the hospital.

At the core of our Voice Communication solution is a patent-protected software platform that we introduced in 2002. We have significantly enhanced and added features and functionality to this solution through ongoing development based on frequent interactions with our customers. Our software platform is built upon a scalable architecture and recognizes more than 100 voice commands. Users can instantly communicate with others using the Vocera communication badge, or through Vocera Connect client applications available for BlackBerry, iPhone and Android smartphones, as well as Cisco wireless IP phones and other mobile devices. Our Voice Communication solution can also be integrated with nurse call and other clinical systems to immediately and efficiently alert hospital workers to patient needs. Since inception we have shipped over 500,000 communication badges to our customers.

We outsource the manufacturing of our products. Our outsourced manufacturing model allows us to scale our business without the significant capital investment and on-going expenses required to establish and maintain manufacturing operations. We work closely with our contract manufacturer, SMTC Corporation and key suppliers to manage the procurement, quality and cost of components. We seek to maintain an optimal level of finished goods inventory to meet our forecast sales and unanticipated shifts in sales volume and mix.

Our diverse customer base ranges from large hospital systems to small local hospitals, as well as other healthcare facilities and customers in non-healthcare markets. We have very low customer revenue concentrations. Our largest end-customers represented only 1.9% and 2.7% of revenue for the three months ended March 31, 2013 and the year ended 2012, respectively. While we have international customers in other English speaking countries such as Canada, the United Kingdom and Australia, most of our customers are located in the United States. International customers represented 11.4% and 10.7% of our revenue in the three months ended March 31, 2013 and the year ended 2012, respectively. We are developing plans to expand our presence in other English speaking markets and enter

non-English speaking markets.
To date, substantially all of our revenue has been derived from sales of our Voice Communication solution, including product maintenance and related services. Revenue declined 3.1% from $23.1 million for the three months ended March 31, 2012 to $22.4 million for the three months ended March 31, 2013. For the three months ended March 31, 2013, we recorded a net loss of $3.5 million.

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We believe uncertainty surrounding the effects of the sequestration and healthcare reform act is affecting all our customers, both government and non-government, and reducing our ability to forecast near-term results. The primary impact this is having on our business is elongating the sales cycle. In the first quarter of 2013, none of the new government purchase orders we had been waiting for were received. While we continue to be disappointed with the pace of getting these new government contracts finalized, we expect that these delayed orders are all still included in the new federal budget.

In addition, several large expansions we had expected to close in the first quarter of 2013 were not consummated, including some sizeable expansion orders that were expected to both book and ship within the quarter. We have increasingly found that health systems have put in place large expense reduction initiatives as a result of healthcare reform, resulting in exceptionally high scrutiny for hospitals' capital budgets.

The number of new hospital accounts added in the first quarter of 2013 was the strongest since 2009, with customer additions from a wide variety of health systems in all parts of the country. These all came from the private sector, as no new federal hospitals were signed in the first quarter. Although not all such new accounts contributed to first quarter 2013 revenues, adding these new customers early in the year should benefit our 2013 results, as well as allowing us to significantly increase our presence in those hospitals over time.

Critical Accounting Policies and Estimates

There have been no changes to our critical accounting policies and estimates as compared to the critical accounting policies and estimates described in our Annual Report on Form 10-K for the year ended December 31, 2012.

Components of operating results

Revenue. We generate revenue from the sale of products and services. Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collection is probable. Revenue is comprised of the following:

- Product. Our solutions include both hardware and software. We refer to hardware revenue as device revenue, which includes revenue from sales of our communication badges, badge accessories, including batteries, battery chargers, lanyards, clips and other ancillary badge components, and our Vocera smartphone. Software revenue is derived primarily from the sale of perpetual licenses to our Voice Communication solution. We derive additional software revenue from the sale of term licenses which can be renewed on a subscription basis. Product revenue is generally recognized upon shipment of hardware and perpetual licenses and, in the case of term licenses, ratably over the applicable term.
- Service. We receive service revenue from sales of software maintenance, extended warranties and professional services. Software maintenance is typically invoiced annually in advance, recorded as deferred revenue and recognized as revenue ratably over the service period. Our professional services revenue is based on both time and materials, and fixed price contracts, and is recognized as the services are provided. Extended warranties are invoiced in advance, recorded as deferred revenue and recognized ratably over the extended warranty period.

Cost of revenue. Cost of revenue is comprised of the following:

- Cost of product. Cost of product is comprised primarily of materials costs, software license costs, warranty and manufacturing overhead for test engineering, material requirements planning and our shipping and receiving functions. Cost of product also includes facility costs, information technology costs and write-offs for excess and obsolete inventory, as well as depreciation and amortization expenses. As we introduce new products, we expect material costs will increase as a percent of revenue for a period of time.
- Cost of service. Cost of service is comprised primarily of employee wages, benefits and related personnel expenses of our technical support team, our professional consulting personnel and our training teams. Cost of service also includes facility and information technology costs. We expect our cost of service will increase as we continue to invest in support services to meet the needs of our customer base.

Operating expenses. Operating expenses are comprised of the following:

- Research and development. Research and development expenses consist primarily of employee wages, benefits and related personnel expenses, hardware materials and consultant fees and expenses related to the design, development, testing and enhancements of our solutions. We intend to continue to invest in improving the functionality of our solutions and the development of new solutions. As a result, we expect research and development expense to increase for the foreseeable future.

Sales and marketing. Sales and marketing expenses consist primarily of employee wages, benefits and related personnel expenses, as well as trade shows, marketing and public relations programs and advertising. Sales commissions are earned

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when an order is received from a customer and, as a result, in some cases these commissions are expensed in an earlier period than the period in which the related revenue is recognized. Historically, our bookings have tended to peak in the fourth quarter of each year driving higher sales commissions, and to be lowest in the first quarter. We intend to continue to expand our direct sales force for the foreseeable future and, accordingly, expect sales and marketing expenses to increase.

- General and administrative. General and administrative expenses consist primarily of employee wages, benefits and related personnel expenses, consulting, audit fees, legal fees and other general corporate expenses. We expect general and administrative expense to increase for the foreseeable future due to the significant costs we expect to incur as we continue to build and maintain the infrastructure necessary to comply with the regulatory requirements of being a public company and as we add personnel to support our growth.

Interest income, interest expense and other expense, net.

- Interest income. Interest income consists primarily of interest income earned on our cash and cash equivalent balances. Our interest income will vary each reporting period depending on our average cash and cash equivalent balances during the period and market interest rates.
- Interest expense. Interest expense includes interest expense related to debt and financing obligations.
- Other income (expense), net. Other income (expense), net consisted primarily of a stipend for market research regarding the industry in which our company operates that we provided to a market research firm, and the change in the fair value of our convertible preferred stock warrants. Our convertible preferred stock warrants were classified as liabilities and, as such, were marked-to-market at each balance sheet date with the corresponding gain or loss from the adjustment recorded as other income (expense), net. Upon the consummation of the initial public offering, on April 2, 2012, these warrants converted into warrants to purchase common stock and are no longer marked-to-market. Other income (expense), net also includes any foreign exchange gains and losses.

Provision for income taxes. We are subject to income taxes in certain countries where we sell our solutions. We anticipate that in the future as we expand our sale of solutions to customers outside the United States, we may become subject to taxation based on the foreign statutory rates in additional countries where these sales take place and our effective tax rate could fluctuate accordingly. Currently, each of our international subsidiaries is operating under cost plus agreements where the U.S. parent company reimburses the international subsidiary for its costs plus an arm's length profit.

Income taxes are computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances have been established to reduce deferred tax assets to the amount reasonably expected to be realized. Changes in valuation allowances are reflected as component of provision for income taxes.

At March 31, 2013, we had a valuation allowance against our deferred tax assets. While we generated pretax profit in 2012, our management believes it is appropriate to obtain confirmatory evidence that our results of operations will sustain this profitability in 2013, before reversing a portion of the valuation allowance to earnings.

We will review on a quarterly basis our conclusions about the appropriate amount of its deferred income tax asset valuation allowance. If we generate profits in 2013, it is likely that the US valuation allowance position may be reversed in the foreseeable future. We expect a significant benefit in the period the valuation allowance reversal is recorded and a significantly higher effective tax rate in periods following the valuation allowance reversal.

Results of Operations

The following table presents our results of operations for the periods indicated. The period-to-period comparisons of results are not necessarily indicative of results for future periods.

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	Three months ended March 31,			
	2013		2012	
(in thousands)	(unaudited)			
Consolidated statement of operations data:	Amount	% Revenue	Amount	% Revenue
Revenue				
Product	$12,960	57.8 %	$14,637	63.3 %
Service	9,453	42.2	8,482	36.7
Total revenue	22,413	100.0	23,119	100.0
Cost of revenues				
Product	4,610	20.6	5,429	23.5
Service	4,084	18.2	3,569	15.4
Total cost of revenues	8,694	38.8	8,998	38.9
Gross profit	13,719	61.2	14,121	61.1
Operating expenses:				
Research and development	3,614	16.1	2,511	10.9
Sales and marketing	10,232	45.7	7,530	32.6
General and administrative	3,298	14.7	3,087	13.4
Total operating expenses	17,144	76.5	13,128	56.8
(Loss) income from operations	(3,425)	(15.3)	993	4.3
Interest income	24	0.1	12	0.1
Interest expense	—	—	(71)	(0.3)
Other expense	(47)	(0.2)	(1,597)	(6.9)
Loss before income taxes	(3,448)	(15.4)	(663)	(2.9)
Provision for income taxes	(51)	(0.2)	(173)	(0.7)
Net loss	$(3,499)	(15.6)%	$(836)	(3.6)%

Comparison of the three months ended March 31, 2013 and 2012

Revenue:

	Three months ended March 31,			
	2013	2012	Change	
(in thousands)	Amount	Amount	Amount	%
Product revenue				
Devices	$9,942	$10,353	$(411)	(4.0)%
Software	3,018	4,284	(1,266)	(29.6)
Total product	12,960	14,637	(1,677)	(11.5)
Service revenue				
Maintenance and support	7,344	6,110	1,234	20.2
Professional services and training	2,109	2,372	(263)	(11.1)
Total service	9,453	8,482	971	11.4
Total revenue	$22,413	$23,119	$(706)	(3.1)

Total revenue decreased $0.7 million, or 3.1%, from the three months ended March 31, 2012 to March 31, 2013.

Product revenue decreased $1.7 million, or 11.5%. Device revenue decreased $0.4 million, or 4.0%, and software revenue decreased $1.3 million, or 29.6%. The decrease in device revenue, which related entirely to our Voice Communication solution, was driven primarily by a decrease in unit sales of badges and related accessories from new customers making initial purchases,

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existing customers expanding deployments within their facilities to new departments and users, and customers replacing badges. The list prices for our products did not change substantially from 2012. The decrease in software revenue was mainly a result of a decrease in sales of Voice Communication software licenses, primarily to existing customers to support enterprise expansions. We believe that our revenue for the three months ended March 31, 2013 was adversely affected by certain macro conditions affecting the U.S. healthcare industry. In particular, sales to U.S. federal government customers were adversely affected by the budget sequestration in the first quarter of 2013 and sales to commercial hospitals were adversely affected by these hospitals seeking to reduce costs due to declining utilization and reduced reimbursement rates under the healthcare reform act. In addition we had inconsistent performance across U.S sales regions, resulting in delays in closing certain anticipated expansion orders.

Service revenue increased $1.0 million, or 11.4% from the three months ended March 31, 2012 to March 31, 2013. Software maintenance and support revenue increased $1.2 million, or 20.2%, and professional services and training revenue decreased $0.3 million, or 11.1%. The increase in software maintenance and support revenue was primarily a result of a larger customer base increasing software maintenance revenue by $0.7 million and an increase in extended warranty revenue of $0.5 million. The decrease in professional services and training revenue is due to a decrease in the number of new deployments and expansions of our Voice Communication solution at established customers, which more than offset the initiation of a large number of new customer contracts.

Cost of revenue:

	Three months ended March 31,			
	2013	2012	Change	
	Amount	Amount	Amount	%
Cost of revenue				
Product	$4,610	$5,429	$(819)	(15.1)%
Service	4,084	3,569	515	14.4
Total cost of revenue	$8,694	$8,998	$(304)	(3.4)
Gross margin				
Product	64.4 %	62.9 %	1.5 %	
Service	56.8	57.9	(1.1)	
Total gross margin	61.2	61.1	0.1	

Cost of product revenue decreased $0.8 million, or 15.1%, from the three months ended March 31, 2012 to March 31, 2013. The decrease in cost of product revenue was primarily due to lower unit shipments. Product gross margin as a percentage of revenue increased in the 2013 period compared to the corresponding period in 2012 due to lower manufacturing costs for the B3000 badge. We do not expect the cost to manufacture the B3000 to decline substantially throughout the remainder of 2013.

Cost of service revenue increased $0.5 million, or 14.4%, from the three months ended March 31, 2012 to March 31, 2013. This increase was primarily due to a $0.3 million increase in employee wages and other personnel costs in our services organization to support growth in customer deployments and technical support. Headcount increased from 74 as of March 31, 2012 to 83 as of March 31, 2013.

Operating expenses:

	Three months ended March 31,			
	2013	2012	Change	
	Amount	Amount	Amount	%
Operating expenses:				
Research and development	$3,614	$2,511	$1,103	43.9 %

Sales and marketing	10,232	7,530	2,702	35.9
General and administrative	3,298	3,087	211	6.8
Total operating expenses	$17,144	$13,128	$4,016	30.6

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Research and development expense. Research and development expense increased $1.1 million, or 43.9%, from the three months ended March 31, 2012 to March 31, 2013. This increase was primarily due to a $0.6 million increase in personnel costs and other expenses associated with an increase in headcount from 50 to 59, a $0.1 million increase due to additional external resources for R&D projects, a $0.1 million increase in non-recurring engineering for R&D projects, and a $0.2 million increase in stock-based compensation.

Sales and marketing expense. Sales and marketing expense increased $2.7 million, or 35.9%, from the three months ended March 31, 2012 to March 31, 2013. This increase was primarily due to a $1.3 million increase in employee wages with an increase in headcount from 116 to 145, $0.5 million due to additional travel costs as our sales force becomes more mobile, $0.5 million increase in stock-based compensation, $0.2 million in marketing expenses and $0.1 million increase in outside services.

General and administrative expense. General and administrative expense increased $0.2 million, or 6.8%, from the three months ended March 31, 2012 to March 31, 2013. This increase was due to a $0.5 million increase in stock compensation offset by a decrease of $0.2 million due to audit fees and external recruiting fees.

Other income (expense):

	Three months ended March 31,		
(in thousands)	2013	2012	Change
Interest income	$24	$12	$12
Interest expense	—	(71)	71
Other expense, net	(47)	(1,597)	1,550

Interest income. Interest income increased from the three months ended March 31, 2012 to March 31, 2013 due to higher cash balances.

Interest expense. We did not incur any interest expense in the three months ended March 31, 2013 as we paid down all outstanding debt after completing our initial public offering in 2012.

Other expense, net. The $1.6 million of other expense for the three months ended March 31, 2012 was due primarily to $1.7 million of non-cash interest expense related to outstanding convertible preferred stock warrants. The warrants were converted to common stock in 2012 when we completed our initial public offering.

Liquidity and capital resources

As of March 31, 2013, we had cash and cash equivalents and short-term investments of $126.4 million and no debt borrowings.

On April 2, 2012, we completed our initial public offering in which we and existing stockholders sold 6,727,500 shares of common stock at $16.00 per share, before underwriting discounts and commissions. We sold 5,000,000 shares and existing stockholders sold an aggregate of 1,727,500 shares, including 877,500 shares as a result of the underwriters' exercise of their over-allotment option. We recorded proceeds of $70.5 million for the IPO, net of offering expenses and underwriters' discounts and commissions. We did not receive any proceeds from the sale of shares by existing stockholders in our initial public offering.

On September 12, 2012, we completed a follow-on public offering in which we and existing shareholders sold 5,548,750 shares of common stock at $28.75 per share, before underwriting discounts and commissions. We sold 1,337,500 shares and existing stockholders sold an aggregate of 4,211,250 shares, including an aggregate of 723,750 shares as a result of the underwriters' exercise of their over-allotment option. We recorded proceeds of approximately $36.0 million, net of offering expenses and underwriters' discounts and commissions. We did not receive any proceeds from the sale of shares by existing stockholders in our follow-on public offering.

On April 3, 2012, we paid in full the outstanding amount under the revolving line of credit. We allowed the line of credit to expire in April 2012.

We believe that our existing sources of liquidity will satisfy our working capital and capital requirements for at least the next twelve months.

(in thousands)	Three months ended March 31, 2013	2012
Consolidated Statements of Cash Flow Data:		
Net cash (used in) provided by operating activities	$(2,186)	$268
Net cash provided by (used in) investing activities	23,469	(545)
Net cash provided by (used in) financing activities	2,603	(468)
Net increase (decrease) in cash and cash equivalents	$23,886	$(745)

Operating activities

Cash used in operating activities was $2.2 million for the three months ended March 31, 2013, due to net loss of $3.5 million, partly offset by exclusion of non-cash items such as depreciation and amortization of $0.5 million for property and equipment and acquired intangible assets and stock-based compensation of $1.7 million. The $6.8 million reduction in accounts receivable was the only significant operating cash inflow, attributable to collections on prior periods' invoices exceeding current periods' billings. This was offset by cash outflows due to a $2.7 million net reduction in accrued bonuses, reflecting year-end bonus payouts and a $1.1 million net reduction in accrued liabilities for ESPP contributions withheld, a $1.8 million increase in inventory due to an $0.8 million finished goods increase in B2000 and B3000 badges as well as an end-of-life memory chip purchase of $0.7 million, a $1.2 million decrease in deferred revenues and a $0.9 million increase in prepaid expense, mainly for insurance and taxes.

Cash provided by operating activities was $0.3 million for the three months ended March 31, 2012, after the exclusion from the net loss of $0.8 million of non-cash items such as the mark to market valuation of the preferred stock warrants of $1.7 million, depreciation and amortization of $0.6 million for property and equipment and acquired intangible assets and stock-based compensation of $0.3 million. These items offset an increase in deferred revenue of $1.0 million, a decrease in accounts payable of $1.9 million due to a pay down of vendor balances from the year end, and a decrease in other assets and liabilities of $0.5 million.

Investing activities

Cash provided by investing activities was $23.5 million for the three months ended March 31, 2013, due to $25.0 million of short-term investment maturities, partly offset by $1.5 million for the purchase of property and equipment and leasehold improvements. The fixed asset purchases included $0.7 million for our ERP implementation project and $0.4 million for our headquarters building expansion.

Cash used in investing activities of $0.5 million for the three months ended March 31, 2012 was due to the purchase of property and equipment and leasehold improvements.

Financing activities

Cash provided by financing activities was $2.6 million for the three months ended March 31, 2013, primarily attributable to $1.6 million from our initial ESPP purchase, as well as $0.4 million from stock option exercises, a $0.3 million reclass of excess tax benefits from stock-based compensation from operating cash flow, $0.2 million from cash exercise of common stock warrants and $0.1 million of cash from lease-related performance obligations.

Cash used in financing activities was $0.5 million for the three months ended March 31, 2012, which was primarily attributable to a $0.5 million decrease in debt due to principal payments being made and $0.3 million of expenses incurred as part of our initial public offering, offset by $0.3 million of proceeds from the exercise of stock options.

Off-Balance Sheet Arrangements

During the three months ended March 31, 2013, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities, that would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The primary objective of our investment activities is to preserve principal while maximizing yields without significantly increasing risk. To achieve this objective, historically we have invested in money market funds. With the proceeds from our two public offerings in 2012, we have invested in a broader portfolio of high credit quality short-term securities. To minimize the exposure due to an adverse shift in interest rates, we maintain an average portfolio duration of one year or less.

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For the initial operation of our portfolio, for the six months ended December 31, 2012 we earned $145,000 of interest income on our cash equivalents and short-term investments, averaging approximately an annual pretax return of 0.3%. Therefore, in the future, if similar invested balances prevailed, a decline in market interest rates from 0.3% to zero would reduce our annual interest income by approximately $0.3 million.

Historically our operations have consisted of research and development and sales activities in the United States. As a result, our financial results have not been materially affected by factors such as changes in foreign currency exchange rates or economic conditions in foreign markets. In the fourth quarter of 2010, we acquired Wallace Wireless, Inc., a company based in Toronto, Canada. At the date of acquisition, this company had 16 employees. We expect to generate future revenue and incur future expenses associated with operating our Canadian subsidiary relating to this acquisition. We are developing plans to expand our international presence. Accordingly, we expect that our exposure to changes in foreign currency exchange rates and economic conditions will increase in future periods.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are designed to ensure that information required to be disclosed by us in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in reports filed under the Exchange Act is accumulated and communicated to management, including principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

As of March 31, 2013 we have carried out an evaluation under the supervision of, and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based on our evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2013.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting which occurred during the period covered by this Quarterly Report on Form 10-Q which has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II: OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we may be involved in lawsuits, claims, investigations and proceedings, consisting of intellectual property, commercial, employment and other matters which arise in the ordinary course of business. We are not currently involved in any material legal proceedings.

Item 1A. Risk Factors

Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information set forth in this Quarterly Report on Form 10-Q. Our business, financial condition, results of operations or future prospects could be materially and adversely harmed if any of the following risks, or other risks or uncertainties that are not yet identified or that we currently believe are immaterial, actually occur. The trading price of our common stock could decline due to any of these risks or uncertainties, and, as a result, you may lose all or part of your investment.

Risks related to our business and industry

We have incurred significant losses in the past, and may experience losses in the future. As a result, our business may be harmed and our stock price could decline.

Although we reported net income for the year ended December 31, 2012, we have incurred significant losses in the past and reported a net loss of $3.5 million for the three months ended March 31, 2013. As of March 31, 2013, we had an accumulated

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deficit of $57.5 million. We expect our expenses to increase due to the hiring of additional personnel and the additional operational and reporting costs associated with being a public company. If we cannot return to profitability in 2013, our business may be harmed and our stock price could further decline.

Our ability to be profitable in the future depends upon continued demand for our communication solutions from existing and new customers. Further market adoption of our solutions, including increased penetration within our existing customers, depends upon our ability to improve patient safety and satisfaction and increase hospital efficiency and productivity. In addition, our profitability will be affected by, among other things, our ability to execute on our business strategy, the timing and size of orders, the pricing and costs of our solutions, and the extent to which we invest in sales and marketing, research and development and general and administrative resources.

We depend on sales of our Voice Communication solution in the healthcare market for substantially all of our revenue, and any decrease in its sales would harm our business.

To date, substantially all of our revenue has been derived from sales of our Voice Communication solution to the healthcare market and, in particular, hospitals. Any decrease in revenue from sales of our Voice Communication solution would harm our business. Sales of our Voice Communication solution to the healthcare market accounted for 91% and 92% of our revenue for the three months ended March 31, 2013 and the year ended 2012, respectively. In addition, we obtained a significant portion of these sales from existing hospital customers. We anticipate that sales of our Voice Communication solution will represent a significant portion of our revenue for the foreseeable future. While we are evaluating new solutions for non-healthcare markets, we may not be successful in applying our technology in all of these markets. In any event, we do not anticipate that sales of our Voice Communication solution in non-healthcare markets will represent a significant portion of our revenue for the foreseeable future.

Our success depends in part upon the deployment of our Voice Communication solution by new hospital customers, the expansion and upgrade of our solution at existing customers, and our ability to continue to provide on a timely basis cost-effective solutions that meet the requirements of our hospital customers. Our Voice Communication solution requires a substantial upfront investment by customers. Typically, our hospital customers initially deploy our solution for specific users in specific departments before expanding our solution into other departments or for other users. The cost of the initial deployment depends on the number of users and departments involved, the size and age of the hospital and the condition of the existing wireless infrastructure, if any, within the hospital.

Even if hospital personnel determine that our Voice Communication solution provides compelling benefits over their existing communications methods, their hospitals may not have, or may not be willing to spend, the resources necessary to install and maintain wireless infrastructure to initially deploy and support our solution or expand our solution to other departments or users. Hospitals are currently facing significant budget constraints, ever increasing demands from a growing number of patients and impediments to obtaining reimbursements for their service. In addition, hospitals, including both governmental and non-governmental customers, are experiencing budgeting issues due to the ongoing effects of and uncertainty around the U.S. government sequestration and debt ceiling issues, and as a consequence, we may continue to experience a slowdown and deferral of orders for our Voice Communication solution that could negatively impact our sales. We believe hospitals are currently allocating funds for capital and infrastructure improvements to benefit from recently enacted electronic medical records incentives, which may impact their ability to purchase and deploy our solution. We might not be able to sustain or increase our revenue from sales of our Voice Communication solution, or achieve the growth rates that we envision, if hospitals continue to face significant budgetary constraints and reduce their spending on communications systems.

Our sales cycle can be lengthy and unpredictable, which may cause our revenue and operating results to fluctuate significantly.

Our sales cycles can be lengthy and unpredictable. Our sales efforts involve educating our customers about the use and benefits of our solutions, including the technical capabilities of our solutions and the potential cost savings and productivity gains achievable by deploying them. Customers typically undertake a significant evaluation process, which frequently involves not only our solutions but also their existing communications methods and those of our competitors, and can result in a lengthy sales cycle of nine to twelve months or more. We spend substantial time, effort and money in our sales efforts without any assurance that our efforts will produce any sales. In addition, purchases of our solutions are frequently subject to budget constraints, multiple approvals, and unplanned administrative, processing and other delays. As a result, our revenue and operating results may vary significantly from quarter to quarter.

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If our business does not grow as we expect, or we are not able to manage our growth effectively, our operating results will suffer.

We have experienced significant revenue growth in a short period of time. For example, our revenue increased from $41.1 million for year ended December 31, 2009 to $101.0 million for the year ended December 31, 2012, and over this four-year period, we significantly expanded our operations and more than doubled the number of our employees from 129 as of December 31, 2008 to 343 as of December 31, 2012. Our rapid growth has placed, and will continue to place, a significant strain on our management systems, infrastructure and other resources. We plan to hire additional direct sales and marketing personnel domestically and internationally, acquire complementary businesses, technologies or assets, and increase our investment in research and development. Our future operating results depend to a large extent on our ability to successfully implement these plans and manage our anticipated expansion. To do so successfully we must, among other things:

- manage our expenses in line with our operating plans and current business environment;
- maintain and enhance our operational, financial and management controls, reporting systems and procedures;
- integrate acquired businesses, technologies or assets;
- manage operations in multiple locations and time zones; and
- develop and deliver new solutions and enhancements to existing solutions efficiently and reliably.

We expect to incur costs associated with the investments made to support our growth before the anticipated benefits or the returns are realized, if at all. If we are unable to manage our growth effectively, we may not be able to take advantage of market opportunities or develop new solutions or enhancements to existing solutions. We may also fail to satisfy customer requirements, maintain quality, execute our business plan or respond to competitive pressures, which could result in lower revenue and a decline in the share price of our common stock.

Our revenue and operating results have fluctuated, and are likely to continue to fluctuate, which may make our quarterly results difficult to predict, cause us to miss analyst expectations and cause the price of our common stock to decline.

Our operating results may be difficult to predict, even in the near term, and are likely to fluctuate as a result of a variety of factors, many of which are outside of our control. We have historically obtained substantially all of our revenue from the sale of our Voice Communication solution, which we anticipate will represent the most significant portion of our revenue for the foreseeable future, as we only began offering our Secure Messaging and Care Transition solutions in the last two years.

Comparisons of our revenue and operating results on a period-to-period basis may not be meaningful. You should not rely on our past results as an indication of our future performance. Each of the following factors, among others, could cause our operating results to fluctuate from quarter to quarter:

- the financial health of our healthcare customers and budgetary constraints on their ability to upgrade their communications;
- changes in the regulatory environment affecting our healthcare customers, including impediments to their ability to obtain reimbursement for their services;
- our ability to expand our sales and marketing operations;
- the procurement and deployment cycles of our healthcare customers and the length of our sales cycles;
- variations in the amount of orders booked in a prior quarter but not delivered until later quarters;
- our mix of solutions and pricing, including discounts by us or our competitors;
- our ability to forecast demand and manage lead times for the manufacture of our solutions; and
- our ability to develop and introduce new solutions and features to existing solutions that achieve market acceptance.

Developments in the healthcare industry and governing regulations could negatively affect our business.

Substantially all of our revenue is derived from customers in the healthcare industry, in particular, hospitals. The healthcare industry is highly regulated and is subject to changing political, legislative, regulatory and other influences. Developments generally affecting the healthcare industry, including new regulations or new interpretations of existing regulations, could adversely affect spending on information technology and capital equipment by reducing funding, changes in healthcare pricing or delivery or creating impediments for obtaining healthcare reimbursements, thereby causing our sales to decline and negatively impacting our business. For example, the profit margins of our hospital customers are modest and pending changes in reimbursement for healthcare costs may reduce the overall solvency of our customers or cause further deterioration in their financial or business condition.

In March 2010, the United States enacted comprehensive healthcare reform legislation through the Patient Protection and Affordable Health Care for America Act and the Health Care and Education Reconciliation Act. By some estimates, the new

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law is expected to increase the number of Americans with health insurance coverage by approximately 32 million through individual and employer mandates, subsidies offered to lower income individuals with smaller employers and broadening of Medicaid eligibility, and to affect healthcare reimbursement levels for healthcare providers. We cannot predict with certainty what the ultimate effect of federal healthcare reform or any future legislation or regulation, or healthcare initiatives, if any, implemented at the state level, will have on us or our customers. For example, the federal healthcare reform imposed a 2.3% excise tax on medical devices beginning January 2013, to which our company will be subject if any of our communications solutions are classified as medical devices. The impact of the tax, coupled with reform-associated payment reductions to Medicare and Medicaid reimbursement, could harm our business, operating results and cash flows.

In addition, our customers' expectations regarding pending or potential industry developments may also affect their budgeting processes and spending plans with respect to our communications solutions. The healthcare industry has changed significantly in recent years and we expect that significant changes will continue to occur. However, the timing and impact of developments in the healthcare industry are difficult to predict. We cannot assure you that the markets for our solutions will continue to exist at current levels or that we will have adequate technical, financial and marketing resources to react to changes in those markets.

If we fail to increase market awareness of our brand and solutions, and expand our sales and marketing operations, our business could be harmed.

We intend to continue to add personnel and resources in sales and marketing as we focus on expanding awareness of our brand and solutions and capitalize on sales opportunities with new and existing customers. Our efforts to improve sales of our solutions will result in an increase in our sales and marketing expense and general and administrative expense, and these efforts may not be successful. Some newly hired sales and marketing personnel may subsequently be determined to be unproductive and have to be replaced, resulting in operational and sales delays and incremental costs. If we are unable to significantly increase the awareness of our brand and solutions or effectively manage the costs associated with these efforts, our business, financial condition and operating results could be harmed.

If we fail to offer high-quality services and support for any of our solutions, our ability to sell those solutions will be harmed.

Our ability to sell our Voice Communication, Secure Messaging or Care Transitions solutions is dependent upon our professional services and technical support teams providing high-quality services and support. Our professional services team assists our customers with their wireless infrastructure assessment, clinical workflow design, communication solution configuration, training and project management during the pre-deployment and deployment stages. Once our solutions are deployed within a customer's facility, the customer typically depends on our technical support team to help resolve technical issues, assist in optimizing the use of our solutions and facilitate adoption of new functionality. If we do not effectively assist our customers in deploying our solutions, succeed in helping our customers quickly resolve technical and other post-deployment issues, or provide effective ongoing support services, our ability to expand the use of our solutions with existing customers and to sell our solutions to new customers will be harmed. If deployment of our solutions is unsatisfactory, as has been the case with certain third-party deployments in the past, we may incur significant costs to attain and sustain customer satisfaction. As we rapidly hire new services and support personnel, we may inadvertently hire underperforming people who will have to be replaced, or fail to effectively train such employees, leading in some instances to slower growth, additional costs and poor customer relations. In addition, the failure of channel partners to provide high-quality services and support in markets outside the United States could also harm sales of our solutions.

The implementation of our new enterprise resource planning system could disrupt our business and adversely affect our financial results.

In the fourth quarter of 2012, we began the implementation of our solution for a new enterprise resource planning application, or ERP. We expect to go live with the new system in the second half of 2013. We may experience difficulties in implementing the ERP, and we may fail to obtain the risk mitigation benefits that the implementation is designed to produce. The implementation could also be disruptive to our operations, including the ability to timely ship and track product orders to our customers, project inventory requirements, manage our supply chain and otherwise adequately service our customers.

We depend on a number of sole source and limited source suppliers, and if we are unable to source our components from them, our business and operating results could be harmed.

We depend on sole and limited source suppliers for several hardware components of our Voice Communication solution, including our batteries and integrated circuits. We purchase inventory generally through individual purchase orders. Any of

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these suppliers could cease production of our components, experience capacity constraints, material shortages, work stoppages, financial difficulties, cost increases or other reductions or disruptions in output, cease operations or be acquired by, or enter into exclusive arrangements with, a competitor. These suppliers typically rely on purchase orders rather than long-term contracts with their suppliers, and as a result, even if available, the supplier may not be able to secure sufficient materials at reasonable prices or of acceptable quality to build our components in a timely manner. Any of these circumstances could cause interruptions or delays in the delivery of our solutions to our customers, and this may force us to seek components from alternative sources, which may not have the required specifications, or be available in time to meet demand or on commercially reasonable terms, if at all. Any of these circumstances may also force us to redesign our solutions if a component becomes unavailable in order to incorporate a component from an alternative source.

Our solutions incorporate multiple software components obtained from licensors on a non-exclusive basis, such as voice recognition software, software supporting the runtime execution of our software platform, and database and reporting software. Our license agreements can be terminated for cause. In many cases, these license agreements specify a limited term and are only renewable beyond that term with the consent of the licensor. If a licensor terminates a license agreement for cause, objects to its renewal or conditions renewal on modified terms and conditions, we may be unable to obtain licenses for equivalent software components on reasonable terms and conditions, including licensing fees, warranties or protection from infringement claims. Some licensors may discontinue licensing their software to us or support of the software version used in our solutions. In such circumstances, we may need to redesign our solutions at substantial cost to incorporate alternative software components or be subject to higher royalty costs. Any of these circumstances could adversely affect the cost and availability of our solutions.

Third-party licensors generally require us to incorporate specific license terms and conditions in our agreements with our customers. If we are alleged to have failed to incorporate these license terms and conditions, we may be subject to claims by these licensors, incur significant legal costs defending ourselves against such claims and, if such claims are successful, be subject to termination of licenses, monetary damages, or an injunction against the continued distribution of one or more of our solutions.

Because we depend upon a contract manufacturer, our operations could be harmed and we could lose sales if we encounter problems with this manufacturer.

We do not have internal manufacturing capabilities and rely upon a contract manufacturer, SMTC Corporation, to produce the primary hardware component of our Voice Communication solution. We have entered into a manufacturing agreement with SMTC that is terminable by either party with advance notice and that may also be terminated for a material uncured breach. We also rely on original design manufacturers, or ODMs, to produce accessories, including batteries, chargers and attachments. If SMTC or an ODM is unable or unwilling to continue manufacturing components of our solutions in the volumes that we require, fails to meet our quality specifications or significantly increases its prices, we may not be able to deliver our solutions to our customers with the quantities, quality and performance that they expect in a timely manner. As a result, we could lose sales and our operating results could be harmed.
SMTC or ODMs may experience problems that could impact the quantity and quality of components of our Voice Communication solution, including disruptions in their manufacturing operations due to equipment breakdowns, labor strikes or shortages, component or material shortages and cost increases. SMTC and these ODMs generally rely on purchase orders rather than long-term contracts with their suppliers, and as a result, may not be able to secure sufficient components or other materials at reasonable prices or of acceptable quality to build components of our solutions in a timely manner. The majority of the components of our Voice Communication solution are manufactured in Asia or Mexico and adverse changes in political or economic circumstances in those locations could also disrupt our supply and quality of components of our solutions. In October 2011, we introduced the B3000 badge. Initial

production of this product commenced with SMTC in the United States, and new production fully transitioned to Mexico in May 2012.

Companies occasionally encounter unexpected difficulties in ramping up production of new products, and we may experience such difficulties with future generations of our products. SMTC and our ODMs also manufacture products for other companies. Generally, our orders represent a relatively small percentage of the overall orders received by SMTC and these ODMs from their customers; therefore, fulfilling our orders may not be a priority in the event SMTC or an ODM is constrained in its ability to fulfill all of its customer obligations. In addition, if SMTC or an ODM is unable or unwilling to continue manufacturing components of our solutions, we may have to identify one or more alternative manufacturers. The process of identifying and qualifying a new contract manufacturer or ODM can be time consuming, and we may not be able to substitute suitable alternative manufacturers in a timely manner or at an acceptable cost. Additionally, transitioning to a new manufacturer may cause us to incur additional costs and delays if the new manufacturer has difficulty manufacturing components of our solutions to our specifications or quality standards.

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If we fail to forecast our manufacturing requirements accurately, or fail to properly manage our inventory with our contract manufacturer, we could incur additional costs and experience manufacturing delays, which can adversely affect our operating results.

We place orders with our contract manufacturer, SMTC, and we and SMTC place orders with suppliers based on forecasts of customer demand. Because of our international low cost sourcing strategy, our lead times are long and cause substantially more risk to forecasting accuracy than would result were lead times shorter. Our forecasts are based on multiple assumptions, each of which may introduce errors into our estimates affecting our ability to meet our customers' demands for our solutions. We also may face additional forecasting challenges due to product transitions in the components of our solutions, or to our suppliers discontinuing production of materials and subcomponents required for our solutions. If demand for our solutions increases significantly, we may not be able to meet demand on a timely basis, and we may need to expend a significant amount of time working with our customers to allocate limited supply and maintain positive customer relations, or we may incur additional costs in order to source additional materials and subcomponents to produce components of our solutions or to expedite the manufacture and delivery of additional inventory. If we underestimate customer demand, our contract manufacturer may have inadequate materials and subcomponents on hand to produce components of our solutions, which could result in manufacturing interruptions, shipment delays, deferral or loss of revenue, and damage to our customer relationships. Conversely, if we overestimate customer demand, we and SMTC may purchase more inventory than required for actual customer orders, resulting in excess or obsolete inventory, thereby increasing our costs and harming our operating results.

If hospitals do not have and are not willing to install, upgrade and maintain the wireless infrastructure required to effectively operate our Voice Communication solution, then they may experience technical problems or not purchase our solution at all.

The effectiveness of our Voice Communication solution depends upon the quality and compatibility of the communications environment that our healthcare customers maintain. Our solutions require voice-grade wireless, or Wi-Fi, installed through large enterprise environments, which can vary from hospital to hospital and from department to department within a hospital. Many hospitals have not installed a voice-grade wireless infrastructure. If potential customers do not have a wireless network that can properly and fully interoperate with our Voice Communication solution, then such a network must be installed, or an existing Wi-Fi network must be upgraded or modified, for example, by adding access points in stairwells, for our Voice Communication solution to be fully functional. The additional cost of installing or upgrading a Wi-Fi network may dissuade potential customers from installing our solution. Furthermore, if changes to a customer's physical or information technology environment cause integration issues or degrade the effectiveness of our solution, or if the customer fails to upgrade or maintain its environment as may be required for software releases or updates or to ensure our solution's effectiveness, the customer may not be able to fully utilize our solution or may experience technical problems, or these changes may impact the performance of other wireless equipment being used. If such circumstances arise, prospective customers may not purchase or existing customers may not expand their use of or deploy upgraded versions of our Voice Communication solution, thereby harming our business and operating results.

If we fail to achieve and maintain certification for certain U.S. federal standards, our sales to U.S. government customers will suffer.

We believe that a significant opportunity exists to sell our products to healthcare facilities in the Veterans Administration and Department of Defense, or DoD. These customers require independent certification of compliance with particular requirements relating to encryption, security, interoperability and scalability. These requirements include compliance with Federal Information Processing Standard, or FIPS, 140-2 and, as to DoD facilities, certification by the Joint Interoperability and Test Command of DoD and under the DoD Information Assurance

Certification and Accreditation Process. We have received certification under certain of these standards for a military-specific configuration of the Vocera communication solution incorporating the B2000 badge. We are carrying out activities intended to achieve additional certifications, including certifications applicable to the B3000 badge and future products as well. A failure on our part to comply in a timely manner with these requirements, or to maintain certification, both as to current products and as to new product versions, could adversely impact our revenue.

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Our Mobility Business Unit may not be successful in selling our communications solutions in non-healthcare markets.

Our primary focus has been on selling our communications solutions to the healthcare market, with other markets addressed only opportunistically. We recently created our Mobility Business Unit for sales efforts to customers outside the healthcare market, and it will initially focus on customers in selected industries. We may not be successful in further penetrating the non-healthcare markets upon which we are initially focusing, or other new markets. Our Voice Communication solution has been deployed in over 200 customers in non-healthcare markets, including hospitality, retail and libraries. Total revenue from non-healthcare customers accounted for 3% of our revenue in the three months ended March 31, 2013 and 3% of our revenue in the year ended 2012, respectively. If we cannot maintain these customers by providing communications solutions that meet their requirements, if we cannot successfully expand our communications solutions in non-healthcare markets, or if our solutions are adopted more slowly than we anticipate, we may not obtain significant revenue from these markets. We may experience challenges as we expand in non-healthcare markets, including pricing pressure on our solutions and technical issues as we adapt our solutions for the requirements of new markets. Our communications solutions also may not contain the functionality required by these non-healthcare markets or may not sufficiently differentiate us from competing solutions such that customers can justify deploying our solutions.

If we fail to successfully develop and introduce new solutions and features to existing solutions, our revenue, operating results and reputation could suffer.

Our success depends, in part, upon our ability to develop and introduce new solutions and features to existing solutions that meet existing and new customer requirements. We may not be able to develop and introduce new solutions or features on a timely basis or in response to customers' changing requirements, or that sufficiently differentiate us from competing solutions such that customers can justify deploying our solutions. We may experience technical problems and additional costs as we introduce new features to our software platform, deploy future models of our wireless badges and integrate new solutions with existing customer clinical systems and workflows. In addition, we may face technical difficulties as we expand into non-English speaking countries and incorporate non-English speech recognition capabilities into our Voice Communication solution. Our B3000 badge, introduced in late 2011, has reduced demand for our existing B2000 badges, and we must therefore successfully manage the transition from existing badges, avoid excessive inventory levels and ensure that sufficient supplies of new badges can be delivered to meet customer demand. We also may incur substantial costs or delays in the manufacture of the B3000 badge and any additional new products or models as we seek to optimize production methods and processes at our contract manufacturer. In addition, we expect that we will at least initially achieve lower gross margins on new models, while endeavoring to reduce manufacturing costs over time. If any of these problems were to arise, our revenue, operating results and reputation could suffer.

If we do not achieve the anticipated strategic or financial benefits from our acquisitions or if we cannot successfully integrate them, our business and operating results could be harmed.

We have acquired, and in the future may acquire, complementary businesses, technologies or assets that we believe to be strategic, such as our four acquisitions completed in 2010. We may not achieve the anticipated strategic or financial benefits, or be successful in integrating any acquired businesses, technologies or assets. If we cannot effectively integrate our Voice Communication solution with our Secure Messaging and Care Transition solutions and successfully market and sell these solutions, we may not achieve market acceptance for, or significant revenue from, these new solutions.

Integrating newly acquired businesses, technologies and assets could strain our resources, could be expensive and time consuming, and might not be successful. Our 2010 acquisitions exposed us and we will be further exposed, if we acquire or invest in additional businesses, technologies or assets, to a number of risks, including that we may:

- experience technical issues as we integrate acquired businesses, technologies or assets into our existing communications solutions;
- encounter difficulties leveraging our existing sales and marketing organizations, and direct sales channels, to increase our revenue from acquired businesses, technologies or assets;
- find that the acquisition does not further our business strategy, we overpaid for the acquisition or the economic conditions underlying our acquisition decision have changed;
- have difficulty retaining the key personnel of acquired businesses;
- suffer disruption to our ongoing business and diversion of our management's attention as a result of transition or integration issues and the challenges of managing geographically or culturally diverse enterprises; and
- experience unforeseen and significant problems or liabilities associated with quality, technology and legal contingencies relating to the acquisition, such as intellectual property or employment matters.

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In addition, from time to time we may enter into negotiations for acquisitions that are not ultimately consummated. These negotiations could result in significant diversion of management time, as well as substantial out-of-pocket costs. If we were to proceed with one or more significant acquisitions in which the consideration included cash, we could be required to use a substantial portion of our available cash. To the extent we issue shares of capital stock or other rights to purchase capital stock, including options and warrants, the ownership of existing stockholders would be diluted. In addition, acquisitions may result in the incurrence of debt, contingent liabilities, large write-offs, or other unanticipated costs, events or circumstances, any of which could harm our operating results.

We generally recognize revenue from maintenance and support contracts over the contract term, and changes in sales may not be immediately reflected in our operating results.

We generally recognize revenue from our customer maintenance and support contracts ratably over the contract term, which is typically 12 months, in some cases subject to an early termination right. Revenue from our maintenance and support contracts accounted for 32.8% and 26.0% of our revenue for the three months ended March 31, 2013 and the year ended 2012, respectively. A portion of the revenue we report in each quarter is derived from the recognition of deferred revenue relating to maintenance and support contracts entered into during previous quarters. Consequently, a decline in new or renewed maintenance and support by our customers in any one quarter may not be immediately reflected in our revenue for that quarter. Such a decline, however, will negatively affect our revenue in future quarters. Accordingly, the effect of significant downturns in sales and market acceptance of our services and potential changes in our rate of renewals may not be fully reflected in our operating results until future periods.

The failure of our equipment lease customers to pay us under leasing agreements with them that we do not sell to third party lease finance companies could harm our revenue and operating results.

In 2012 we began offering our badges and related hardware accessories to our customers through multi-year equipment lease agreements. For a sale, we recognize product-related revenue at the net present value of the lease payment stream once our obligations related to such sale have been met. We plan to sell the bulk of these leases, including the related accounts receivables, to third party lease finance companies on a non-recourse basis. We will have to retain unsold leases in-house, which will expose us to the creditworthiness of such equipment lease customers over the lease term. For the leases that we retain in-house, our ability to collect payments from a customer or to recognize revenue for the sale could be impaired if the customer fails to meet its obligations to us such as in the case of its bankruptcy filing or deterioration in its financial position, or has other creditworthiness issues, any of which could harm our revenue and operating results.

Our success depends upon our ability to attract, integrate and retain key personnel, and our failure to do so could harm our ability to grow our business.

Our success depends, in part, on the continuing services of our senior management and other key personnel, and our ability to continue to attract, integrate and retain highly skilled personnel, particularly in engineering, sales and marketing. Competition for highly skilled personnel is intense, particularly in the Silicon Valley where our headquarters are located. If we fail to attract, integrate and retain key personnel, our ability to grow our business could be harmed.

The members of our senior management and other key personnel are at-will employees, and may terminate their employment at any time without notice. If they terminate their employment, we may not be able to find qualified individuals to replace them on a timely basis or at all and our senior management may need to divert their attention from other aspects of our business. Former employees may also become employees of a competitor. We may also have to pay additional compensation to attract and retain key personnel. We also anticipate hiring additional engineering, marketing and sales, and services personnel to grow our business. Often, significant amounts of time and resources are required to train these personnel. We may incur significant costs to attract, integrate and retain them, and we may lose them to a competitor or another company before we realize the benefit of our investments in them.

We primarily compete in the rapidly evolving and competitive healthcare market, and if we fail to effectively respond to competitive pressures, our business and operating results could be harmed.

We believe that at this time the primary competition for our Voice Communication solution consists of traditional methods using wired phones, pagers and overhead intercoms. While we believe that our system is superior to these legacy methods, our solution requires a significant infrastructure investment by a hospital and many hospitals may not recognize the value of implementing our solution.

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Manufacturers and distributors of product categories such as cellular phones, pagers, mobile radios and in-building wireless telephones attempt to sell their products to hospitals as components of an overall communication system. Of these product categories, in-building wireless telephones represent the most significant competition for the sale of our solution. The market for in-building wireless phones is dominated by large horizontal communications companies such as Cisco Systems, Ascom and Polycom, which sold its Spectralink wireless phones business to a Sun Capital Partners' affiliate in December 2012. In addition, while smartphones and tablets are not at present direct competitors, their proliferation may make them a de facto standard for hospital workflow, thereby making our solution less attractive to customers.

While we do not have a directly comparable competitor that provides a richly featured voice communication system for the healthcare market, we could face such competition in the future. Potential competitors in the healthcare or communications markets include large, multinational companies with significantly more resources to dedicate to product development and sales and marketing. These companies may have existing relationships within the hospital, which may enhance their ability to gain a foothold in our market. Customers may prefer to purchase a more highly integrated or bundled solution from a single provider or an existing supplier rather than a new supplier, regardless of performance or features. Accordingly, if we fail to effectively respond to competitive pressures, we could experience pricing pressure, reduced profit margins, higher sales and marketing expenses, lower revenue and the loss of market share, any of which would harm our business, operating results or financial condition.

Our international operations subject us, and may increasingly subject us in the future, to operational, financial, economic and political risks abroad.

Although we derive a relatively small portion of our revenue from customers outside the United States, we believe that non-U.S. customers could represent an increasing share of our revenue in the future. During the three months ended March 31, 2013 and the year ended 2012, we obtained 11.4% and 10.7% of our revenue, respectively, from customers outside of the United States, including Canada, the United Kingdom, Australia, the Republic of Ireland and New Zealand. Accordingly, we are subject to risks and challenges that we would not otherwise face if we conducted our business solely in the United States, including:

- challenges incorporating non-English speech recognition capabilities into our solutions as we expand into non-English speaking jurisdictions;
- difficulties integrating our solutions with wireless infrastructures with which we do not have experience;
- difficulties integrating local dialing plans and applicable PBX standards;
- challenges associated with delivering support, training and documentation in several languages;
- difficulties in staffing and managing personnel and resellers;
- the need to comply with a wide variety of foreign laws and regulations, including increasingly stringent data privacy regulations, requirements for export controls for encryption technology, employment laws, changes in tax laws and tax audits by government agencies;
- political and economic instability in, or foreign conflicts that involve or affect, the countries of our customers;
- difficulties in collecting accounts receivable and longer accounts receivable payment cycles;
- exposure to competitors who are more familiar with local markets;
- limited or unfavorable intellectual property protection in some countries; and
- currency exchange rate fluctuations, which could affect the price of our solutions relative to locally produced solutions.

Any of these factors could harm our existing international business, impair our ability to expand into international markets or harm our operating results.

Our Voice Communication solution is highly complex and may contain undetected software or hardware errors that could harm our reputation and operating results.

Our Voice Communication solution incorporates complex technology, is deployed in a variety of complex hospital environments and must interoperate with many different types of devices and hospital systems. While we test the components of our solutions for defects and errors prior to release, we or our customers may not discover a defect or error until after we have deployed our solution, integrated it into the hospital environment and our customer has commenced general use of the solution. For example, in 2005, a prior model of our wireless badge, the B1000, was affected by chipset compatibility issues with certain wireless access points at customer facilities, resulting in our exchanging a large percentage of deployed badges for new badges. We did this exchange at no cost to our customers, thereby incurring substantial costs. In addition, our solutions in some cases are integrated with hardware and software offered by “middleware” vendors in order to interoperate with nurse call systems, device alarms and other hospital systems. If we cannot successfully integrate our solution with these vendors as needed or if any hardware or software of these vendors contains any defect or error, then our solution may not perform as

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designed, or may exhibit a defect or error.

Any defects or errors in, or which are attributed to, our solutions, could result in:

- delayed market acceptance of our affected solutions;
- loss of revenue or delay in revenue recognition;
- loss of customers or inability to attract new customers;
- diversion of engineering or other resources for remedying the defect or error;
- damage to our brand and reputation;
- increased service and warranty costs; and
- legal actions by our customers and hospital patients, including product liability claims.

If any of these occur, our operating results and reputation could be harmed.

We face potential liability related to the privacy and security of personal information collected through our solutions.

In connection with our healthcare communications business, we handle and have access to personal health information subject in the United States to the Health Insurance Portability and Accountability Act of 1996, or HIPAA, the Health Information Technology for Economic and Clinical Health Act of 2009, or HITECH, regulations issued pursuant to these statutes, state privacy and security laws and regulations, and associated contractual obligations as a “business associate” of healthcare providers. These statutes, regulations and contractual obligations impose numerous requirements regarding the use and disclosure of personal health information with which we must comply. Our failure to accurately anticipate the application or interpretation of these statutes, regulations and contractual obligations as we develop our solutions, a failure by us to comply with their requirements (e.g., evolving encryption and security requirements) or an allegation that defects in our products have resulted in noncompliance by our customers could create material civil and/or criminal liability for us, resulting in adverse publicity and negatively affecting our business.

In addition, the use and disclosure of personal health information is subject to regulation in other jurisdictions in which we do business or expect to do business in the future. Those jurisdictions may attempt to apply such laws extraterritorially or through treaties or other arrangements with U.S. governmental entities. We might unintentionally violate such laws, such laws may be modified and new laws may be enacted in the future which may increase the chance that we violate them. Any such developments, or developments stemming from enactment or modification of other laws, or the failure by us to comply with their requirements or to accurately anticipate the application or interpretation of these laws could create material liability to us, result in adverse publicity and negatively affect our business.

For example, the European Union, or EU, adopted the Data Protection Directive, or DPD, imposing strict regulations and establishing a series of requirements regarding the storage of personally identifiable information on computers or recorded on other electronic media. This has been implemented by all EU member states through national laws. DPD provides for specific regulations requiring all non-EU countries doing business with EU member states to provide adequate data privacy protection when receiving personal data from any of the EU member states. Similarly, Canada’s Personal Information and Protection of Electronic Documents Act provides Canadian residents with privacy protections in regard to transactions with businesses and organizations in the private sector and sets out ground rules for how private sector organizations may collect, use and disclose personal information in the course of commercial activities. A finding that we have failed to comply with applicable laws and regulations regarding the collection, use and disclosure of personal information could create liability for us, result in adverse publicity and negatively affect our business.

Any legislation or regulation in the area of privacy and security of personal information could affect the way we operate our services and could harm our business. The costs of compliance with, and the other burdens imposed by, these and other laws or regulatory actions may prevent us from selling our solutions or increase the costs associated with selling our solutions, and may affect our ability to invest in or jointly develop solutions in the United States and in foreign jurisdictions. Further, we cannot assure you that our privacy and security policies and practices will be found sufficient to protect us from liability or adverse publicity relating to the privacy and security of personal information.

Our use of open source and non-commercial software components could impose risks and limitations on our ability to commercialize our solutions.

Our solutions contain software modules licensed under open source and other types of non-commercial licenses, including the GNU Public License, the GNU Lesser Public License, the Apache License and others. We also may incorporate open source and other licensed software into our solutions in the future. Use and distribution of such software may entail greater risks than use of third-party commercial software, as licenses of these types generally do not provide warranties or other contractual

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protections regarding infringement claims or the quality of the code. Some of these licenses require the release of our proprietary source code to the public if we combine our proprietary software with open source software in certain manners. This could allow competitors to create similar products with lower development effort and time and ultimately result in a loss of sales for us.

The terms of many open source and other non-commercial licenses have not been judicially interpreted and there is a risk that such licenses could be construed in a manner that could impose unanticipated conditions or restrictions on our ability to commercialize our solutions. In such event, in order to continue offering our solutions, we could be required to seek licenses from alternative licensors, which may not be available on a commercially reasonable basis or at all, to re-engineer our solutions or to discontinue the sale of our solutions in the event we cannot obtain a license or re-engineer our solutions on a timely basis, any of which could harm our business and operating results. In addition, if an owner of licensed software were to allege that we had not complied with the conditions of the corresponding license agreement, we could incur significant legal costs defending ourselves against such allegations. In the event such claims were successful, we could be subject to significant damages, be required to disclose our source code, or be enjoined from the distribution of our solutions.

Claims of intellectual property infringement could harm our business.

Vigorous protection and pursuit of intellectual property rights has resulted in protracted and expensive litigation for many companies in our industry. Although claims of this kind have not materially affected our business to date, there can be no assurance of the absence of such claims in the future. Any claims or proceedings against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time, result in the diversion of significant operational resources, or require us to enter into royalty or licensing agreements, any of which could harm our business and operating results.

Intellectual property lawsuits are subject to inherent uncertainties due to the complexity of the technical issues involved, and we cannot be certain that we will be successful in defending ourselves against intellectual property claims. In addition, we currently have a limited portfolio of issued patents compared to many other industry participants, and therefore may not be able to effectively utilize our intellectual property portfolio to assert defenses or counterclaims in response to patent infringement claims or litigation brought against us by third parties. Further, litigation may involve patent holding companies or other adverse patent owners who have no relevant products and against whom our potential patents may provide little or no deterrence.

Many potential litigants have the capability to dedicate substantially greater resources to enforce their intellectual property rights and to defend claims that may be brought against them. Furthermore, a successful claimant could secure a judgment that requires us to pay substantial damages or prevents us from distributing certain solutions or performing certain services. We might also be required to seek a license and pay royalties for the use of such intellectual property, which may not be available on commercially acceptable terms or at all. Alternatively, we may be required to develop non-infringing technology, which could require significant effort and expense and may ultimately not be successful.

If we are unable to protect our intellectual property rights, our competitive position could be harmed or we could be required to incur significant expenses to enforce our rights.

Our success depends, in part, on our ability to protect our proprietary technology. We protect our proprietary technology through patent, copyright, trade secret and trademark laws in the United States and similar laws in other countries. We also protect our proprietary technology through licensing agreements, nondisclosure agreements and other contractual provisions. These protections may not be available in all cases or may be inadequate to prevent our competitors from copying, reverse engineering or otherwise obtaining and using our technology, proprietary rights or solutions in an unauthorized manner. The laws of some foreign countries may not be as protective of intellectual property rights as those in the United States, and mechanisms for enforcement of intellectual property rights may be inadequate. In addition, third parties may seek to challenge, invalidate or circumvent our patents, trademarks, copyrights and trade secrets, or applications for any of the foregoing. Our competitors may independently develop technologies that are substantially equivalent, or superior, to our technology or design around our proprietary rights. In each case, our ability to compete could be significantly impaired.

To prevent unauthorized use of our intellectual property rights, it may be necessary to prosecute actions for infringement or misappropriation of our proprietary rights. Any such action could result in significant costs and diversion of our resources and management's attention, and there can be no assurance that we will be successful in such action. Furthermore, many of our current and potential competitors have the ability to dedicate substantially greater resources to enforce their intellectual property rights than us. Accordingly, despite our efforts, we may not be able to prevent third parties from infringing or

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misappropriating our intellectual property. While we plan to continue to protect our intellectual property with, among other things, patent protection, there can be no assurance that:

- current or future U.S. or foreign patent applications will be approved;
- our issued patents will protect our intellectual property and not be held invalid or unenforceable if challenged by third parties;
- we will succeed in protecting our technology adequately in all key jurisdictions in which we or our competitors operate; or
- others will not independently develop similar or competing products or methods or design around any patents that may be issued to us.

Our failure to obtain patents with claims of a scope necessary to cover our technology, or the invalidation of our patents, or our inability to protect any of our intellectual property, may weaken our competitive position and harm our business and operating results. We might be required to spend significant resources to monitor and protect our intellectual property rights. We may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Any litigation, whether or not it is resolved in our favor, could result in significant expense to us and divert the efforts of our technical and management personnel, which may harm our business, operating results and financial condition.

Our solutions could be subject to regulation by the U.S. Food and Drug Administration or similar foreign agencies, which could increase our operating costs.

We provide devices that may be, or may become, subject to regulation by the U.S. Food and Drug Administration, or FDA, and similar agencies in other countries, or the jurisdiction of these agencies could be expanded in the future to include our solutions. The FDA regulates certain products, including software-based products, as “medical devices” based, in part, on the intended use of the product and the risk the device poses to the patient should the device fail to perform properly. Although we have concluded that our wireless badge is a general-purpose communications device not subject to FDA regulation, the FDA could disagree with our conclusion, or changes in our solutions or the FDA’s evolving regulation could lead to FDA regulation of our solutions. Many other countries in which we sell or may sell our solutions could also have similar regulations applicable to our solutions, some of which may be subject to change or interpretation. We may incur substantial operating costs if we are required to register our solutions or components of our solutions as regulated medical devices under U.S. or foreign regulations, obtain premarket approval from the FDA or foreign regulatory agencies, and satisfy the extensive reporting requirements. In addition, failure to comply with these regulations could result in enforcement actions and monetary penalties.

Product liability or other liability claims could cause us to incur significant costs, adversely affect the sales of our solutions and harm our reputation.

Our solutions are utilized by healthcare professionals and others in the course of providing patient care. It is possible that patients, family members, physicians, nurses or others may allege we are responsible for harm to patients or healthcare professionals due to defects in, the malfunction of, the characteristics of, or the operation of, our solutions. Any such allegations could harm our reputation and ability to sell our solutions.

Components of our solutions utilizing Wi-Fi also emit radio frequency, or RF, energy. RF emissions have been alleged, in connection with cellular phones, to have adverse health consequences. While these components of our solutions comply with guidelines applicable to such emissions, some may allege that these components of our solutions cause adverse health consequences or applicable guidelines may change making these components of our solutions non-compliant. Regulatory agencies in the United States and other countries in which we do or plan to do business may implement regulations concerning RF emissions standards. In addition, healthcare professionals have alleged and may allege in the future that magnets in our badges may emit electromagnetic radiation or otherwise interfere with implanted medical or other devices. Any such allegations or non-compliance, or any regulatory developments, including any changes affecting the transmission of radio signals, could negatively impact the sales of our solutions, require costly modifications to our solutions and harm our reputation.

Although our customer agreements contain terms and conditions, including disclaimers of liability, that are intended to reduce or eliminate our potential liability, we could be required to spend significant amounts of management time and resources to defend ourselves against product liability, tort, warranty or other claims. If any such claims were to prevail, we could be forced to pay damages, comply with injunctions or stop distributing our solutions. Even if potential claims do not result in liability to us, investigating and defending against these claims could be expensive and time consuming and could divert management's attention away from our business. We maintain general liability insurance coverage, including coverage for errors and omissions; however, this coverage may not be sufficient to cover large claims against us or otherwise continue to be available on acceptable terms. Further, the insurer could attempt to disclaim coverage as to any particular claim.

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Our business is subject to the risks of earthquakes, fire, floods and other natural catastrophic events, and to interruption by man-made problems such as power disruptions or terrorism.

Our corporate headquarters are located in the San Francisco Bay Area, a region known for seismic activity, and many critical components of our solutions are sourced in Asia and Mexico, regions known to suffer natural disasters. A significant natural disaster, such as an earthquake, fire or a flood, occurring at our headquarters, our other facilities or where our contract manufacturer or its suppliers are located, could harm our business, operating results and financial condition. In addition, acts of terrorism could cause disruptions in our business, the businesses of our customers and suppliers, or the economy as a whole. We also rely on information technology systems to communicate among our workforce located worldwide, and in particular, our senior management, general and administrative, and research and development activities that are coordinated with our corporate headquarters in the San Francisco Bay Area. Any disruption to our internal communications, whether caused by a natural disaster or by man-made problems, such as power disruptions, in the San Francisco Bay Area, Asia or Mexico could delay our research and development efforts, cause delays or cancellations of customer orders or delay deployment of our solutions, which could harm our business, operating results and financial condition.

We may require additional capital to support our business growth, and such capital may not be available.

We intend to continue to make investments to support business growth and may require additional funds to respond to business challenges, which include the need to develop new solutions or enhance existing solutions, enhance our operating infrastructure, expand our sales and marketing capabilities, expand into non-healthcare markets, and acquire complementary businesses, technologies or assets. Accordingly, we may need to engage in equity or debt financing to secure funds. Equity and debt financing, however, might not be available when needed or, if available, might not be available on terms satisfactory to us. If we raise additional funds through equity financing, our stockholders may experience dilution. Debt financing, if available, may involve covenants restricting our operations or our ability to incur additional debt. If we are unable to obtain adequate financing or financing on terms satisfactory to us, our ability to continue to support our business growth and to respond to business challenges could be significantly limited as we may have to delay, reduce the scope of or eliminate some or all of our initiatives, which could harm our operating results.

As an “emerging growth company” under the JOBS Act, we are permitted to, and may, rely on exemptions from certain disclosure and governance requirements.

As an “emerging growth company” under the Jumpstart Our Business Startups Act, or JOBS Act, we are permitted to, and may, rely on exemptions from certain disclosure and governance requirements. For example, for so long as we are an emerging growth company, which can last, at most, until the first fiscal year following the fifth anniversary of our initial public offering, we will not be required to:

- have our independent registered public accounting firm report on our internal control over financial reporting pursuant to Section 404(b) of the Sarbanes-Oxley Act;
- comply with any requirement that may be adopted by the Public Company Accounting Oversight Board regarding mandatory audit firm rotation or a supplement to the auditor's report providing additional information about the audit and the financial statements;
- provide the “compensation discussion and analysis” and certain compensation tables for our named executive officers in our Form 10-K or annual proxy statement; and
- submit certain executive compensation matters to stockholder advisory votes, such as “say on pay” and “say on frequency.”

We could be an emerging growth company for up to five years, although, if the market value of our common stock that is held by non-affiliates exceeds $700 million as of June 30 of any year starting with June 30, 2013, we could cease to be an “emerging growth company” as of the following December 31. Thereafter, as of each fiscal year end, our independent registered public accounting firm will be required to evaluate and report on our internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act. While management has established plans to accommodate the additional assessment and attestation procedures and related costs of Section 404(b) compliance, we may incur additional costs or require additional management time to comply with Section 404(b) in a timely manner. To the extent we find a material weakness or other deficiency in our internal control over financial reporting, the accuracy and timeliness of our financial reporting may be adversely affected.

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If we do not maintain effective internal control over financial reporting or disclosure controls and procedures in the future, the accuracy and timeliness of our financial reporting may be adversely affected.

The Sarbanes-Oxley Act requires, among other things, that we assess the effectiveness of our internal control over financial reporting annually and disclosure controls and procedures quarterly. In particular, beginning with the year ending on December 31, 2013, we must obtain reasonable assurance of our internal control over financial reporting to allow management to report on the effectiveness of our internal control over financial reporting as required by Section 404 of the Sarbanes-Oxley Act. If a material weakness in our internal control over financial reporting is identified in the future, we are not able to comply with the requirements of Section 404 in a timely manner or we do not maintain effective controls, our reported financial results could be materially misstated or could be restated, we could receive an adverse opinion regarding our controls from our independent registered public accounting firm (once such opinion is required under the Sarbanes-Oxley Act), we could be subject to investigations or sanctions by regulatory authorities, which would require additional financial and management resources, and the market price of our stock could decline.

We will continue to incur increased costs as a result of operating as a public company and our management will have to devote substantial time to public company compliance obligations.

As a public company, we will continue to incur substantial legal, accounting and other expenses that we did not incur as a private company. We will continue to incur substantial expenses even though we as an “emerging growth company” may rely upon the disclosure and governance exemptions under the JOBS Act. The Sarbanes-Oxley Act of 2002, or Sarbanes-Oxley Act, as well as rules subsequently implemented by the SEC and our stock exchange, impose various requirements on public companies, including changes in corporate governance practices. Our management and other personnel will need to devote a substantial amount of time to these compliance requirements and any new requirements that the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 may impose on public companies. Moreover, these rules and regulations, along with compliance with accounting principles and regulatory interpretations of such principles, as amended by the JOBS Act, have increased and will continue to increase our legal, accounting and financial compliance costs and have made and will continue to make some activities more time-consuming and costly. For example, we expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantial costs to maintain the same or similar coverage.

Compliance with the SEC's new rule for disclosures on sourcing of "conflict minerals" will likely be time consuming and potentially costly and could adversely affect our reputation.

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the SEC has adopted a new rule that applies to companies that use certain minerals and metals, known as conflict minerals, in their products, including certain products manufactured for them by third parties. The new rule will require companies that use conflict minerals in the production of their products to conduct diligence as to whether or not such minerals originate from the Democratic Republic of Congo and adjoining countries and to file certain information with the SEC about the use of these minerals. We will incur additional costs to comply with the due diligence and disclosure requirements. In addition, depending upon our findings, or our inability to make reliable findings, about the source of any conflict minerals that we use, our reputation could be harmed. While the first report is not due until 2014, we will need to incur costs in preparation for this reporting in 2013. Certain industry organizations have filed a petition challenging the adoption of the new rule by the SEC, but we are unable to predict the impact of this challenge on the applicability of the new rule.

Risks related to our common stock

The market price of our common stock may be volatile, and your investment in our stock could suffer a decline in value.

There has been significant volatility in the market price and trading volume of equity securities, which is often unrelated or disproportionate to the financial performance of the companies issuing the securities. These broad market fluctuations may negatively affect the market price of our common stock. The market price of our common stock could fluctuate significantly in response to the factors described in this "Risk Factors" section and elsewhere in this Form 10-Q and other factors, many of which are beyond our control, including:

- actual or anticipated variation in anticipated operating results of us or our competitors;
- the financial projections we may provide to the public, any changes in these projections or our failure to meet these projections;
- announcements by us or our competitors of new solutions, new or terminated significant contracts, commercial relationships or capital commitments;
- failure of securities analysts to maintain coverage of us, changes in financial estimates by any securities analysts who

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follow our company, or our failure to meet these estimates or the expectations of investors;
- developments or disputes concerning our intellectual property or other proprietary rights;
- commencement of, or our involvement in, litigation;
- announced or completed acquisitions of businesses, technologies or assets by us or our competitor;
- changes in operating performance and stock market valuations of other technology companies generally, or those in our industry in particular;
- price and volume fluctuations attributable to inconsistent trading volume levels of our common stock;
- our public float relative to the total number of shares of our common stock that are issued and outstanding;
- price and volume fluctuations in the overall stock market, including as a result of trends in the economy as a whole;
- rumors and market speculation involving us or other companies in our industry;
- any major change in our management;
- unfavorable economic conditions and slow or negative growth of our markets; and
- other events or factors, including those resulting from war or incidents of terrorism.

In addition, in the past, following periods of volatility in the overall market and the market price of a particular company’s securities, securities class action litigation has often been instituted against these companies. This litigation, if instituted against us, could result in substantial costs and a diversion of our management's attention and resources.

If securities or industry analysts issue an adverse or misleading opinion regarding our stock or do not publish research or reports about our business, our stock price could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us and our business. We do not control these analysts or the content and opinions included in their reports. The price of our common stock could decline if one or more analysts downgrade our common stock or if those analysts issue other unfavorable commentary or cease publishing reports about us or our business. If one or more analysts cease coverage of our company or fail to regularly publish reports about our company, we could lose visibility in the financial market, which in turn could cause our stock price to decline. Further, securities or industry analysts may elect not to provide research coverage of our common stock and such lack of research coverage may adversely affect the market price of our common stock.

The concentration of our capital stock ownership with insiders will likely limit your ability to influence corporate matters.

Our executive officers, directors, current 5% or greater stockholders and entities affiliated with any of them together beneficially own approximately 43% of our common stock outstanding as of March 31, 2013. These stockholders, if they act together, will have significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, and may take actions that may not be in the best interests of our other stockholders. This concentration of ownership could also limit stockholders’ ability to influence corporate matters. Accordingly, corporate actions might be taken even if other stockholders, including you, oppose them, or may not be taken even if other stockholders view them as in the best interests of our stockholders. This concentration of ownership may have the effect of delaying or preventing a change of control of our company, may make the approval of certain transactions difficult or impossible without the support of these stockholders and might adversely affect the market price of our common stock.

Our management has broad discretion over the use of proceeds from our public offerings and might not apply the proceeds of our public offerings in ways that increase the value of your investment in our company.

Our management has broad discretion to use the net proceeds to us from our initial public offering and our secondary public offering, and you are relying on the judgment of our management regarding the application of these proceeds, without the opportunity to assess whether the proceeds are being used appropriately. The failure of our management to apply the $70.5 million net proceeds of our initial public offering and the $36.0 million net proceeds from our secondary public offering effectively could harm our business, financial condition and operating results, and may not increase the value of your investment in our company. Largely as a result of these public offerings, we had $126.4 million invested in cash, cash equivalents, and short-term investments as of March 31, 2013. We have not allocated these net proceeds for specific purposes other than allocating a portion of the proceeds from our initial public offering to the repayment in full of outstanding borrowings under our credit facility, which we repaid in April 2012. We intend to use the net proceeds from our public offerings for general corporate and working capital purposes. We may also use a portion of the net proceeds to acquire or invest in complementary businesses, technologies or assets, but at this time, we have no current understandings, agreements or commitments to do so. Our management might not be able to yield a significant return or any return on any investment of these net proceeds.

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Our stock price could decline due to the substantial number of outstanding shares of our common stock that are available for sale on the public market.

All of our outstanding shares recently became freely tradable without restrictions or further registration under the federal securities laws, except for shares held by directors, executive officers and other affiliates which are subject to volume limitations under Rule 144 of the Securities Act of 1933 and various vesting agreements. If the holders of the shares that were previously subject to transfer restrictions sell, or indicate an intention to sell, substantial amounts of our common stock could be available for sale in the public market, and the trading price of our common stock could decline. Additional shares subject to outstanding warrants and shares subject to outstanding options and reserved for future issuance under our stock option and purchase plans could also be available for sale in the public market to the extent permitted by the provisions of various vesting agreements and Rules 144 and 701 under the Securities Act.

We have never paid cash dividends on our capital stock, and we do not anticipate paying any dividends in the foreseeable future.

We have never paid cash dividends on any of our capital stock and currently intend to retain our future earnings to fund the development and growth of our business. As a result, capital appreciation, if any, of our common stock will be the sole source of gain for the foreseeable future.

Our charter documents and Delaware law could discourage, delay or prevent a change of control of our company or change in our management that stockholders consider favorable and cause our stock price to decline.

Certain provisions of our restated certificate of incorporation and restated bylaws and Delaware law could discourage, delay or prevent a change of control of our company or change in our management that the stockholders of our company consider favorable. These provisions:

- authorize the issuance of “blank check” preferred stock that our board of directors could issue to increase the number of outstanding shares and to discourage a takeover attempt;
- prohibit stockholder action by written consent, requiring all stockholder actions to be taken at a meeting of stockholders;
- establish advance notice procedures for nominating candidates to our board of directors or proposing matters that can be acted upon by stockholders at stockholder meetings;
- limit the ability of our stockholders to call special meetings of stockholders;
- prohibit stockholders from cumulating their votes for the election of directors;
- permit newly created directorships resulting from an increase in the authorized number of directors or vacancies on our board of directors to be filled only by majority vote of our remaining directors, even if less than a quorum is then in office;
- provide that our board of directors is expressly authorized to make, alter or repeal our bylaws;
- establish a classified board of directors so that not all members of our board are elected at one time;
- provide that our directors may be removed only for “cause” and only with the approval of the holders of at least 66 2/3rds percent of our outstanding stock; and
- require super-majority voting to amend certain provisions in our certificate of incorporation and bylaws.

Section 203 of the Delaware General Corporation Law may also discourage, delay or prevent a change of control of our company.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Use of Proceeds from Public Offering of Common Stock

None.

Issuer Purchases of Equity Securities

The table below provides information with respect to repurchases of unvested shares of our common stock made pursuant to our 2000 Stock Option Plan, as amended, and our 2006 Stock Option Plan, as amended. All shares in the table below were shares repurchased as a result of us exercising our right of repurchase for unvested shares under our stock option plans and not pursuant to a publicly announced plan or program.

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Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs
January 1- January 31, 2013	763	$ 2.16	—	—
February 1- February 28, 2013	729	2.16	—	—
March 1- March 31, 2013	0	—	—	—
Total	1,492	$ 2.16	—	—

Item 3. Defaults Upon Senior Securities
None.
Item 4. Mine Safety Disclosures
None.
Item 5. Other Information
None.

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Item 6. Exhibits

Exhibit Number	Exhibit title
31.01	Certification of Chief Executive Officer pursuant to Securities Exchange Act Rules 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.02	Certification of Chief Financial Officer pursuant to Securities Exchange Act Rules 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.01+	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS††	XBRL Instance Document
101.SCH††	XBRL Taxonomy Schema Linkbase Document
101.CAL††	XBRL Taxonomy Calculation Linkbase Document
101.DEF††	XBRL Taxonomy Definition Linkbase Document
101.LAB††	XBRL Taxonomy Labels Linkbase Document
101.PRE††	XBRL Taxonomy Presentation Linkbase Document

\+ This certification shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date hereof and irrespective of any general incorporation language in any filings.

†† In accordance with Rule 406T of Regulation S-T, the information in these exhibits is furnished and deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Exchange Act of 1934,as amended, and otherwise is not subject to liability under these sections.

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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.

		VOCERA COMMUNICATIONS, INC.
Date: May 14, 2013	By:	/S/ Robert J. Zollars
		Robert J. Zollars
		Chief Executive Officer
		(Principal Executive Officer)
Date: May 14, 2013	By:	/S/ William R. Zerella
		William R. Zerella
		Chief Financial Officer
		(Principal Financial Officer)

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EXHIBIT INDEX

Exhibit Number	Exhibit title
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