MERGE HEALTHCARE INC
Form 424B5
November 16, 2009

PROSPECTUS SUPPLEMENT
(To Prospectus dated November 5, 2009)

MERGE HEALTHCARE INCORPORATED
9,084,032 Shares of Common Stock

We are selling up to 9,084,032 shares of our common stock. The common stock will be sold at a price of $3.00 per share.

For a more detailed description of our common stock, see the section entitled “Description of Common Stock and Preferred Stock” beginning on page 12 of the accompanying prospectus.

Our common stock is quoted on the Nasdaq Global Market under the symbol “MRGE.” On November 12, 2009, the last reported sale price of our common stock on the Nasdaq Global Market was $3.60 per share.

We have retained William Blair & Company, L.L.C., Robert W. Baird & Co. Incorporated and Craig-Hallum Capital Group LLC to act as exclusive placement agents in connection with this offering. See “Plan of Distribution” beginning on page S-25 of this prospectus supplement for more information regarding these arrangements.

Investing in our securities involves a high degree of risk. See “Risk Factors” beginning on page S-7 of this prospectus supplement.

	Per Share	Total
Public offering price of common stock	$ 3.000	$ 27,252,096
Placement agency fees	$ 0.180	$ 1,635,126
Proceeds, before expenses, to us	$ 2.820	$ 25,616,970

William Blair & Company, L.L.C., Robert W. Baird & Co. Incorporated and Craig-Hallum Capital Group LLC are acting as the placement agents in this offering. The placement agents are not purchasing or selling any of the securities pursuant to this prospectus supplement or the accompanying prospectus. We estimate the total expenses of this offering, excluding the placement agency fees, will be approximately $375,000. Because there is no minimum offering amount required as a condition to closing in this offering, the actual offering amount, the placement agency fees and net proceeds to us, if any, in this offering may be substantially less than the total offering amounts set forth above. We are not required to sell any specific number or dollar amount of the securities offered in this offering, but the placement agent will use its reasonable best efforts to arrange for the sale of all of the securities offered. We currently anticipate that closing of the sale of securities will take place on or about November 18, 2009.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement and the accompanying prospectus are truthful or complete. Any representation to the contrary is a criminal offense.

William Blair & Company
Robert W. Baird & Co. Incorporated
Craig-Hallum Capital Group LLC

The date of this prospectus supplement is November 13, 2009.

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ABOUT THIS PROSPECTUS SUPPLEMENT

This prospectus supplement is a supplement to the accompanying prospectus that is also a part of this document. This prospectus supplement and the accompanying prospectus, dated November 5, 2009, are part of a registration statement on Form S-3 (File No. 333-161691) that we filed with the Securities and Exchange Commission, or the SEC, utilizing a "shelf" registration process. Under this shelf registration process, we may offer and sell from time to time in one or more offerings the securities described in the accompanying prospectus.

This document is in two parts. The first part is this prospectus supplement, which describes the securities we are offering and the terms of the offering and also adds to and updates information contained in the accompanying prospectus and the documents incorporated by reference into the accompanying prospectus. The second part is the accompanying prospectus, which provides more general information, some of which may not apply to the securities offered by this prospectus supplement. Generally, when we refer to this "prospectus," we are referring to both documents combined. To the extent there is a conflict between the information contained in this prospectus supplement, on the one hand, and the information contained in the accompanying prospectus or any document incorporated by reference therein, on the other hand, you should rely on the information in this prospectus supplement. We urge you to carefully read this prospectus supplement and the accompanying prospectus and any related free writing prospectus, together with the information incorporated herein and therein by reference as described under the heading "Where You Can Find More Information," before buying any of the securities being offered.

You should rely only on the information that we have provided or incorporated by reference in this prospectus supplement and the accompanying prospectus and any related free writing prospectus that we may authorize to be provided to you. We have not, and the placement agents have not, authorized anyone to provide you with different information. No other dealer, salesperson or other person is authorized to give any information or to represent anything not contained in this prospectus supplement and the accompanying prospectus or any related free writing prospectus that we may authorize to be provided to you. You must not rely on any unauthorized information or representation. This prospectus supplement is an offer to sell only the securities offered hereby, and only under circumstances and in jurisdictions where it is lawful to do so. You should assume that the information in this prospectus supplement and the accompanying prospectus or any related free writing prospectus is accurate only as of the date on the front of the document and that any information we have incorporated by reference is accurate only as of the date of the document incorporated by reference, regardless of the time of delivery of this prospectus supplement and the accompanying prospectus or any related free writing prospectus, or any sale of a security.

This prospectus supplement contains summaries of certain provisions contained in some of the documents described herein, but reference is made to the actual documents for complete information. All of the summaries are qualified in their entirety by the actual documents. Copies of some of the documents referred to herein have been filed, will be filed or will be incorporated by reference as exhibits to the registration statement of which this prospectus supplement is a part, and you may obtain copies of those documents as described below under the heading "Where You Can Find More Information."

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PROSPECTUS SUPPLEMENT SUMMARY

This summary is not complete and does not contain all of the information that you should consider before investing in the securities offered by this prospectus. You should read this summary together with the entire prospectus supplement and prospectus, including our financial statements, the notes to those financial statements and the other documents that are incorporated by reference in this prospectus supplement, before making an investment decision. See the Risk Factors section of this prospectus supplement on page S-7 for a discussion of the risks involved in investing in our securities. In this prospectus supplement, unless the context otherwise indicates, "we," "us," and "our" refer to Merge Healthcare Incorporated and its subsidiaries.

Our Business

Merge Healthcare Incorporated

Merge Healthcare Incorporated, a Delaware corporation, develops solutions that automate healthcare data and diagnostic workflow to enable a better electronic record of the patient experience, and to enhance product development for health IT, device and pharmaceutical companies and delivers related services. Our products, ranging from standards-based development toolkits to sophisticated clinical applications, have been used by healthcare providers, vendors and researchers worldwide for over 20 years. Our principal executive offices are located at 6737 West Washington Street, Suite 2250, Milwaukee, Wisconsin 53214–5650, and the telephone number there is (414) 977–4000.

Merge Healthcare was founded in 1987 and specialized in the transformation of legacy radiology (film–based) images into filmless digitized images for distribution and diagnostic interpretation. We acquired eFilm Medical Inc. in June 2002 for its diagnostic medical image workstation software capabilities; RIS Logic, Inc. in July 2003 for its RIS software, which manages business and clinical workflow for imaging centers; AccuImage Diagnostics Corp. in January 2005 for its advanced visualization technologies for clinical specialty medical imaging; and Cedara Software Corp. in June 2005, which significantly enhanced our medical imaging software offerings. In 2009, we acquired:

- etrials Worldwide, Inc in July in order to provide clinical trial sponsors and contract research organizations ("CROs") comprehensive and configurable solutions that include both critical imaging technologies and proven eClinical capabilities; and

- Confirma, Inc. in September in order to combine forces in an effort to expand computer aided detection ("CAD") technology.

Our business is health IT software, which can involve any aspect of moving medical images and/or information into electronic media. Our major product categories consist of:

- Software development toolkits and platforms, which give software developers resources to accelerate new product development;

- Diagnostic workstation software applications, which bring specialized reading and review tools to the clinician's desktop;

- RIS and related applications, which manage the business workflow of an imaging enterprise or radiology department;

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- PACS and related applications, which manage the medical image workflow of a healthcare enterprise;

- Surgical Management Systems, which automate the monitoring and recording of anesthesia and perfusion before, during and after a surgery;

- CAD products, which automate the analysis and interventional guidance of studies provided by radiology practices;

- Software-as-a-service ("SaaS"), which includes electronic data capture ("EDC"), interactive voice and Web response ("IVR"/"IWR") and electronic patient diaries ("eDiary") for clinical trial sponsors and CRO's.

- Consultative engineering, which provides customer development teams with added expertise and technology; and

- Managed Services, which extends additional image and remote information management capabilities to our customers.

We generate revenue through licensing software and/or intellectual property, upgrading and/or renewing those licenses, ongoing service and support of the solutions, SaaS delivery of solutions, project or hourly professional services, consultative engineering fees and pay-per-study managed services.

Our technologies and expertise span all the major digital imaging modalities, including computed tomography ("CT"), magnetic resonance imaging ("MRI"), digital x–ray, mammography, ultrasound, echo-cardiology, angiography, nuclear medicine, positron emission tomography ("PET") and fluoroscopy. These offerings are used in all aspects of clinical imaging workflow, including: the display of a patient's digital image; the archiving communication and manipulation of digital images; clinical applications to analyze digital images; and the use of imaging in minimally-invasive surgery. We have continued to innovate with its product lines and has extended its business into new areas of medical imaging.

Our software is deployed in hospitals and clinics worldwide through our partner, direct end-user and eCommerce channels and used by clinical trial sponsors and CRO's worldwide. This software is licensed by many of the world's largest medical device and healthcare information technology companies. With global brand recognition for products such as eFilm Workstation(TM), a downloadable diagnostic imaging application, and MergeCOM-3 DICOM toolkits, we believe we are able to generate a foothold in new international markets upon which it can expand into additional product lines.

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The Offering

Common stock offered by us	Up to 9,084,032 shares
Common stock to be outstanding after this offering	75,211,822 shares
Use of proceeds	We intend to use the net proceeds from this offering to prepay in full our senior secured note due June 2010 (the "Note"), which includes all amounts owed under the Note of $15.0 million and an additional $3.1 million amount due as a result of the prepayment, and for general corporate purposes, including working capital. See "Use of Proceeds" on page S-22.
Market for the common stock	Our common stock is quoted and traded on the Nasdaq Global Market under the symbol "MRGE."
Risk factors	You should read the "Risk Factors" section of this prospectus supplement and in the documents incorporated by reference in this prospectus supplement for a discussion of factors to consider before deciding to purchase our securities.
Nasdaq Global Market trading symbol for common stock	MRGE

The number of shares of common stock to be outstanding after this offering as reflected in the table above is based on the actual number of shares outstanding as of September 30, 2009, which was 66,127,790, and does not include, as of that date:

- 4,853,113 shares of common stock issuable upon the exercise of outstanding options, with a weighted average exercise price of $3.74 per share; and
- 3,982,812 shares of common stock reserved for future issuance under our 1996 Stock Option Plan for Employees of Merge Healthcare Incorporated dated May 13, 1996, as amended and restated in its entirety as of September 1, 2003, 1998 Stock Option Plan for Directors, 2000 Employee Stock Purchase Plan, and 2005 Equity Incentive Plan.

Unless otherwise stated, outstanding share information throughout this prospectus supplement excludes such outstanding options and shares available for issuance.

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RISK FACTORS

Before you make a decision to invest in our securities, you should consider carefully the risks described below, together with other information in this prospectus supplement, the accompanying prospectus and the information incorporated by reference herein and therein. Each of the risks described in these sections and documents incorporated by reference could materially and adversely affect our business, financial condition, results of operations and prospects, and could result in a loss of your investment. If any of the following events actually occur, our business, operating results, prospects or financial condition could be materially and adversely affected. This could cause the trading price of our common stock to decline and you may lose all or part of your investment. The risks described below are not the only ones that we face. Additional risks not presently known to us or that we currently deem immaterial may also significantly impair our business operations and could result in a complete loss of your investment.

Risks Related To The Company

We may not be able to realize the anticipated benefits from our acquisitions of Confirma and etrials.

We may not be able to realize the anticipated benefits from our acquisitions of Confirma and etrials. Achieving those benefits depends on the timely, efficient and successful execution of a number of post-acquisition events, including integrating the businesses of Confirma and etrials into our company. Factors that could affect our ability to achieve these benefits include:

- Difficulties in integrating and managing personnel, financial reporting and other systems used by the businesses of Confirma and etrials into our company;
- The failure of the businesses of Confirma and etrials to perform in accordance with our expectations;
- Any future goodwill impairment charges that we may incur with respect to the assets of Confirma or etrials;
- Failure to achieve anticipated synergies between our business units and the business units of Confirma and etrials;
- The loss of customers; and
- The loss of any of the key managers and employees.

If the businesses of Confirma and etrials do not operate as we anticipate, our business, financial condition and results of operations could be materially harmed. In addition, the loss of any key managers or employees of Confirma or etrials could have a material adverse effect on our business.

In addition, as a result of the acquisitions, we have assumed all of the liabilities of Confirma and etrials. We may learn additional information about the businesses of Confirma and etrials that adversely affects us, such as unknown or contingent liabilities, issues relating to internal controls over financial reporting and issues relating to compliance with the Sarbanes-Oxley Act or other applicable laws. As a result, there can be no assurance that the acquisitions will be successful or will not, in fact, harm our business. Among other things, if liabilities of Confirma and etrials are greater than projected, or if there are obligations of which we were not aware at the time of completion of the acquisition, our business could be materially adversely affected.

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In addition, both Confirma and etrials have accumulated deficits from operations and might never achieve or maintain profitability, which could materially adversely affect our business and operating results.

The successful integration of the businesses of Confirma and etrials into our company will present significant challenges.

We anticipate that the acquisitions of Confirma and etrials will place significant demands on our administrative, operational and financial resources, and we cannot assure you that we will be able to successfully integrate the businesses of Confirma and etrials into our company. Our failure to successfully integrate Confirma and etrials into our company, and to manage the challenges presented by the integration process successfully, may prevent us from achieving the anticipated benefits of the acquisitions and could have a material adverse effect on our business.

Our acquisition of etrials could trigger certain provisions contained in etrials' agreements with third parties that could permit such parties to terminate that agreement.

etrials may be a party to agreements that permit a counter-party to terminate an agreement or receive payments because the acquisition would cause a default or violate an anti-assignment, change of control or similar clause in such agreements. If this happens, we may have to seek to replace that agreement with a new agreement or make additional payments under such agreements. However, we may be unable to replace a terminated agreement on comparable terms or at all. Depending on the importance of such agreement to etrials' business, the failure to replace a terminated agreement on similar terms or at all, and requirements to pay additional amounts, may increase our costs of operating etrials' business or prevent us from operating etrials' business.

We have incurred and will continue to incur significant costs associated with the acquisition of etrials.

We estimate that we or etrials will incur direct transaction costs of approximately $2.8 million associated with the acquisition of etrials, including direct costs of the acquisition as well as liabilities to be accrued in connection with the acquisition (excluding any related severance costs). All such direct acquisition costs will be expensed as incurred. We believe the combined entity may incur charges to operations, which are not currently reasonably estimable, in the quarter in which the acquisition is completed or the following quarters, to reflect costs associated with integrating the two companies. We may incur additional material charges in subsequent quarters to reflect additional costs associated with the acquisition. We anticipate that the combination will require significant cash outflows for acquisition and integration related costs. If the benefits of the acquisition do not exceed the costs of integrating the businesses, our financial results may be adversely affected.

The market price of our common stock may decline as a result of our acquisition of Confirma.

The market price of our common stock could be materially adversely affected as a result of our acquisition of Confirma. Some of the risks that we could face are:

- The integration of Confirma's business is unsuccessful or takes longer or is more disruptive than anticipated;
- We do not achieve the expected synergies or other benefits of the Confirma acquisition as rapidly or to the extent anticipated, if at all;
- The effect of the acquisition of Confirma on our financial results does not meet our expectations; or

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- After the acquisition, Confirma's business does not perform as anticipated.

In connection with the acquisition of Confirma, we issued 5,422,104 additional shares of our common stock. On November 5, 2009, a registration statement governing the resale of these shares became effective with the SEC and therefore these shares will be freely tradable, subject to certain restrictions. The increase in the number of outstanding shares of our Common Stock may lead to sales of such shares or the perception that such sales may occur, either of which may adversely affect the market price of our common stock.

There are a limited number of stockholders who have significant control over our common stock, allowing them to have significant influence over the outcome of all matters submitted to stockholders for approval, which may conflict with our interests and the interests of other stockholders.

Our directors, officers and principal stockholders (stockholders owning 10% or more of our common stock) beneficially owned approximately 30,429,682, or 46.0%, of the outstanding shares of common stock and stock options that could have been converted to common stock at September 30, 2009, and such stockholders will have significant influence over the outcome of all matters submitted to our stockholders for approval, including the election of directors and other corporate actions. In addition, such influence by these affiliates could have the effect of discouraging others from attempting us to take over, thereby increasing the likelihood that the market price of the common stock will not reflect a premium for control.

Our business could be harmed by the deteriorating general economic and market conditions that lead to reduced spending on information technology products.

Our business and operating results might be adversely affected by worldwide economic conditions and, in particular, conditions in the pharmaceutical, biotechnology and medical device industries we serve. As our business expands globally, we have become increasingly subject to the risks arising from adverse changes in domestic and global economic and political conditions. Economic growth in the U.S. and other countries slowed since the second half of 2008, which caused our customers to delay or reduce information technology purchases. As a result of slowing global economic growth, the credit market crisis, declining consumer and business confidence, shifts in consumer spending patterns, increased unemployment, reduced levels of capital expenditures, fluctuating commodity prices, bankruptcies and other challenges currently affecting the global economy, our clients might experience deterioration of their businesses, cash flow shortages, and difficulty obtaining financing. If economic conditions in the U.S. and other countries continue to deteriorate, customers may continue to delay or further reduce purchases. This could result in additional reductions in sales of our products, longer sales cycles, slower adoption of new technologies and increased price competition. In addition, weakness in the end-user market could negatively affect the cash flow of our OEM and VAR customers who could, in turn, delay paying their obligations, which would increase our credit risk exposure and cause a decrease in operating cash flows. Also, if OEM and VAR customers experience excessive financial difficulties and/or insolvency, and we are unable to successfully transition end-users to purchase products from other vendors or directly from us, sales could decline significantly. Any of these events would likely harm our business, results of operations and financial condition.

Continued disruption in credit markets and world-wide economic changes may adversely affect our business, financial condition, and results of operations.

Continued disruptions in the financial and credit markets may adversely affect our business and financial results. The tightening of credit markets may reduce the funds available to our customers to buy our products and services. It may also result in customers extending the length of time in which they pay and in our having higher customer receivables with increased default rates. General concerns about the fundamental soundness of domestic and foreign economies may also cause customers to reduce their purchases, even if they have cash or if credit is available to them.

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Our future capital needs are uncertain and our ability to access additional financing may be negatively impacted by the volatility and disruption of the capital and credit markets and adverse changes in the global economy.

Our capital requirements in the future will depend on many factors, including:

- Acceptance of and demand for our products;
- The extent to which we invest in new technology and product development;
- The costs of developing new products, services or technologies;
- The number and method of financing of acquisitions and other strategic transactions; and
- The costs associated with the growth of our business, if any.

We intend to finance our operations and any growth of our business with existing cash and cash flows from operations. We believe existing cash and anticipated cash flows from operations will be sufficient to meet operating and capital requirements through at least the twelve month period following the filing of this prospectus supplement. If adverse global economic conditions persist or worsen, however, we could experience a decrease in cash flows from operations and may need additional financing to fund operations. Due to the existing uncertainty in the capital markets (including debt, private equity, venture capital and traditional bank lending), access to additional debt or equity may not be available on acceptable terms or at all. If we cannot raise funds on acceptable terms when necessary, we may not be able to develop or enhance products and services, execute our business plan, take advantage of future opportunities or respond to competitive pressures or unanticipated customer requirements.

We may experience significant fluctuations in revenue growth rates and operating results.

We may not be able to accurately forecast our growth rate. We base expense levels and investment plans on sales estimates and currently review all estimates on a quarterly basis. Many of our expenses and investments are fixed and we may not be able to adjust spending quickly enough if sales are lower than expected.

Our revenue growth may not be sustainable and our percentage growth rates may decrease or fluctuate significantly. Our revenue and operating profit growth depends on the continued growth of demand for our products and services offered through us or our OEM and VAR customers, and our business is affected by general economic and business conditions worldwide. A softening of demand, whether caused by changes in customer preferences or a weakening of the U.S. or global economies, may result in decreased revenue or growth.

Our net sales and operating results will also fluctuate for many other reasons, including due to risks described elsewhere in this section and the following:

- Demand for our software solutions and services;
- Our sales cycle;

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- Economic cycles;
- The level of reimbursements to our end-user customers from government sponsored healthcare programs (principally, Medicare and Medicaid);
- Accounting policy changes mandated by regulating entities;
- Delays due to customers' internal budgets and procedures for approving capital expenditures, by competing needs for other capital expenditures and the deployment of new technologies and personnel resources;
- Our ability to retain and increase sales to existing customers, attract new customers and satisfy our customers' demands;
- Our ability to fulfill orders;
- The introduction of competitive products and services;
- Price decreases;
- Changes in the usage of the Internet and eCommerce, including in non-U.S. markets;
- Timing, effectiveness and costs of expansion and changes in our systems and infrastructure;
- The outcomes of legal proceedings and claims involving us; and