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MDRX - Q1 2015 Allscripts Healthcare Solutions Inc Earnings Call

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OVERVIEW:

MDRX reported 1Q15 non-GAAP net income of $15m and non-GAAP diluted EPS of $0.08. Co. expects 2015 revenue to be $1.40-1.43b and non-GAAP EPS to be $0.42-0.50.

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PRESENTATION

Operator

Good afternoon. My name is Wanda, and I will be your conference operator today. At this time, I would like to welcome everyone to the Allscripts first quarter 2015 earnings conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session.

(Operator Instructions)

I would now like to turn the call over to Mr. Seth Frank. Please go ahead, sir.

Seth Frank - *Allscripts Healthcare Solutions Inc - VP of IR*

Good afternoon. Thank you, Wanda. Our speakers on today's call are Paul Black, President and Chief Executive Officer, and Rick Poulton, Allscripts' Chief Financial Officer. Some of the statements that we will make today may be considered forward-looking, including statements regarding future investments and our future performance. These statements involve a number of risks and uncertainties that could cause our results to differ materially from the [actuals].

These forward-looking statements reflect our opinions only as of the date of this presentation, and we undertake no obligation to revise these forward-looking statements in light of new information or future events. Please refer to our filings with the Securities and Exchange Commission for more detailed descriptions of the risk factors that may affect our results. And with that, I'd like to hand the call over to Paul.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Good evening, and thank you for joining the Allscripts first quarter 2015 earnings call. Rick will discuss the financial details shortly. Here are a couple of key highlights. First, we have introduced a simplified financial presentation that we believe will be helpful to all of you going forward. We also think it makes the Allscripts story easier to digest, for those of you in the financial community who are new to the Company.

First-quarter bookings were $236 million, up $13 million, or 6%, year over year. This is an all-time Q1 record for Allscripts. In total, Allscripts added nearly 200 new clients, across all venues of care, during the quarter. As expected, total revenue declined in the quarter, due largely to a reduction in nonrecurring professional services. The revenue decline was in line with what we anticipated and discussed on the Q4 earnings call. We also discussed, at that time, the factors influencing this trajectory.

In contrast, Allscripts' higher margin recurring revenue continues to grow. You can see that trend, more clearly than ever, in the new supplemental data sheet available on the investor section of the Allscripts website. We maintained a tight discipline on operating expenses, which drove an increase in adjusted EBITDA and EPS. I'm also very pleased by the significant cash flow we delivered during the quarter. In short, we've continued to execute the financial play book we spelled out over a year ago, building a strong foundation for value creation among Allscripts clients, associates and shareholders.

Looking at the business in detail, Allscripts' progress with Sunrise for the acute and integrated enterprise markets continues to accelerate. In March, for the second consecutive year, Black Book Market Research named Sunrise the top overall inpatient electronic health records for large hospitals and academic medical centers in 2015. Also during the quarter, KLAS Research named Sunrise as 2014 Best-in-Class global acute EMR, and category leader for global acute EMR in Canada. KLAS also cited the Sunrise client base as being among the most stable in the industry.

Higher levels of third-party recognition and client satisfaction leads to opportunities for market share growth. Today, we are excited to announce two new Sunrise clients. The first, Palo Verde Hospital, is located in east Los Angeles. They offer a full range of services, from maternity to end of life palliative and hospice care. Palo Verde will implement Sunrise acute clinicals and revenue cycle management, and they will adopt value based solutions, including hosting and outsourcing services.

The other new client is Grand Lake Health Systems in Saint Mary's, Ohio. This organization consists of a joint township medical center, plus 14 ambulatory centers. Grand Lake selected Sunrise in a competitive process, after evaluating multiple alternative offerings. Allscripts' ability to deliver a proven single integrated patient record platform for ambulatory, acute, ED, critical care, surgery and revenue cycle was a key factor in their decision. Grand Lake signed with us in the second quarter.

We are pleased with these initial 2015 successes. We expect to maintain this momentum, gaining new Sunrise clients domestically, as the year progresses. Internationally, we remain highly focused on securing new client opportunities in the UK, Canada, Middle East, and the Asia-Pacific marketplace. We did not sign a new international agreement in the first quarter, but are optimistic, with a solid near-term pipeline, as we see increased interest in population health and EMR solutions.

In the ambulatory market, we continue to see a solid growth platform for increased wallet share from two primary areas. One, managed IT services, and two, high value operational services. During the quarter, a longtime TouchWorks client, Healthcare Partners, selected us to provide managed IT services to support a portion of their physician operations. We continue to see opportunities for hosting growth across the pro and TouchWorks ambulatory client base. Operational, high value service offerings include interoperability infrastructure services, revenue cycle management outsourcing, ACO services, revenue for referral and linking solutions, and bundle payment consulting.

We have made significant investments, and are building our capabilities for these high value operational services. Earlier this quarter, we accelerated the introduction of Allscripts outsource revenue cycle management service offerings. We already see a building pipeline of new business in this area, which is based on a percentage of collections business model. Other services target clinical productivity and enhancing revenue, by reducing referral and network leakage to non-network providers. As clients evaluate the opportunity of bundled payment and at-risk, fee-for-value models, many are looking for assistance in optimizing the care and outcomes of chronically ill.

We see additional opportunities in these areas. Turning to population management, we see a shift in client strategy, as they navigate beyond Meaningful Use and ICD-10. We are well positioned for this opportunity. Case in point, the population health interoperability dialogue on the exhibit floor at HIMMS this year was at a fever pitch. While there was a lot of hype about future capabilities, we are generating results with clients today.

We have invested aggressively, and established a strategic leadership position to operationalize population health strategies, implement open systems, and achieve eloquent workflow integration and connectivity across the care continuum. [Our lead] started well over eight years ago, by building an open interoperable ecosystem through our Allscripts developer program. Not only do we provide an open API, we have invested significantly in a robust business model, including executive leadership, a partner portal, technical documentation, testing and development resources, and an application store with 75,000 unique visitors in 2014.

Allscripts has an entire business unit focused on the open platform, to enable partners to be successful, and our clients to innovate. This approach provides a clear and distinguished alternative to the market. As healthcare organizations invest in next-generation connectivity and care coordination solutions for value-based care, they are also looking to preserve capital and achieve a single, community-based patient record, without the unnecessary time, pain and cost of rip and replace. The vision that we bring to the marketplace is grounded in a set of comprehensive capabilities that enable an organization's population health strategy.

Our strategy is called [dbMotion], a comprehensive solution of technology and services that provides an actionable pathway to navigate successfully from fee for service to value-based care models. The objective is to connect and deliver the right data, at the right time, to the right caregiver, anywhere in the care delivery network, while leveraging the robust platform capabilities. Thus matching the right patient the right resource at the right time, facilitating and directing precision transitions of care. Here are a couple of examples of these working live population health management strategies.

A major client in Northern Florida is expanding with Allscripts, implementing dbMotion, Care director and Allscripts Population Health Analytics. This organization is very large, in a densely populated area, with over 1,000 beds and over 40 ambulatory and post-acute facilities. Their strategy is to manage at-risk patients by connecting all employed primary care providers with affiliated non-employed specialists, to enable precision transitions of care. This platform enables actionable, community-wide patient care plans, using Care Director, to manage this polychronic population.

This concept of enabling precision transitions is a critical business driver today. Hospital admissions are declining, while system-wide acuity is increasing. Organizations are seeing an increase in their post-acute census. As a result, healthcare organizations are coordinating care from the home to the clinic to the hospital, to nursing facilities and home care settings. Their focus is to reduce length of stay and preventable re-admissions.

Secondly, a large healthcare system in Chicago is leveraging Allscripts Care Management for precise match of the right patient and resource at the right time, and have expanded their use of Allscripts Home Care for collaborative care coordination across the post-acute network, resulting in a savings of tens of millions of dollars, by driving preventable re-admissions and length of stay down by over 40% and 33%, respectively. As a result, of this market trend, increased client focus and improving solution portfolio, we are seeing some good momentum, both inside and outside the Allscripts core EHR base for our proven solutions.

A few examples from Q1 include the following. The largest Allscripts Care Director agreement in Allscripts history, with a health system in Eastern Pennsylvania. Another dbMotion sale outside Allscripts' EHR base, to a community health system in Indiana. Sunrise client in the Southeast purchased dbMotion to connect its installed third-party ambulatory EHR with Sunrise, and provide a platform for an overall connectivity strategy. And number four, we also had good results this quarter with EPSI, closing new clients and publishing client outcome stories on cost and quality management.

Before turning the call over to Rick, I want to provide our perspective on the industry looking ahead, and how we are poised to capitalize on that opportunity, in light of recent regulatory, legislative and policy activity that impacts the healthcare industry. First, we believe the repeal and replacement of a sustainable growth rate formula for Medicare physician fees likely clears a path towards a healthcare payment system driven by quality and outcomes improvement. This model will likely become the de facto standard for how providers will be compensated under Medicare.

We expect this change will bring providers who have been ineligible to participate in the Meaningful Use program, or who have chosen not to engage, to adopt the healthcare technology more broadly, as they will be compelled to report on the quality of the care they're delivering, and to enable participation in value-based programs. This dovetails with the announcement in January, by CMS, to accelerate Medicare providers to alternative payment models tied to performance. In addition, market-based solutions, such as ACOs and patient-centered medical homes, will likely expand.

We also expect new advanced payment models to be introduced by public and private payers, to try to shift further to a cost sharing environment, where all parties are equally incented to focus on value. With these changes will come an unprecedented need by providers to ensure they track, coordinate and monitor the patient population, clinically and financially, inside the provider's own organization, and where those patients are consuming services outside of the provider's own network. Finally, the proposed rule making for the stage 3 of Meaningful Use was recently published.

We support the government's policy to streamline the program for providers, and focus on the areas that can deliver the most value to healthcare: interoperability and measurable quality improvement. In all, our strategic market position is very good. Focusing on population health as an engine of growth has been beneficial in multiple ways. When you combine this success with the gains of Sunrise, global expansion, and enviable ambulatory presence, the emergence of new value-added services, we have multiple paths to sustainable growth over the coming years. And with that, I will turn the call over to Rick.

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Okay. Thanks very much, Paul, and good afternoon everybody. As I review the first-quarter results, please reference both our GAAP financial statements, as well as the non-GAAP tables in our Earnings Release, and also the supplemental data sheets that we posted to our Investor Relations section of our website a little earlier this afternoon. As Paul mentioned, we're pleased to provide you with a new financial statement presentation that we believe both simplifies and makes more informative, and more aligns with how our business has evolved. And it's much easier, we think, to digest than our previous presentation.

Considering this change, it's more important than ever to review the supplemental data this quarter, and this document has been revised to complement and enhance the new revenue presentation. The supplemental data sheet includes a bifurcation of bookings, backlog, revenue, and gross profit, by the two new revenue categories, on the face of our first-quarter income statement. As well as, it drills down into recurring and nonrecurring revenue by quarter, on a historic basis. Any information from prior periods has been recast to conform with this new presentation, just so you have consistency.

So let me start with an overview of the quarter. Looking at Q1 financials, overall, our results were largely in line with what we previewed during our fourth-quarter call that we hosted earlier this year. As Paul noted, bookings started the year off on a very solid footing, with 6% year-over-year growth. Our recurring revenue grew 3% on a year-over-year basis, and gross margins in our recurring revenue areas remained very strong and very stable. Total revenue declined on an overall basis, due to a decrease in nonrecurring revenue, predominantly in our project-based professional services, which are now a part of other client services on our supplemental data sheet.

As we had projected on our last call, these services declined approximately $8 million from Q4 levels. Weaker system sales also contributed to our overall revenue decline, as demand for hardware was soft, and our clients continue to prefer to purchase software on a subscription basis. But notwithstanding this weaker overall revenue, we maintained a strong focus on our discretionary spending. And as a result, we grew our non-GAAP operating income, our adjusted EBITDA, and our non-GAAP EPS, year over year, despite this revenue decline.

And lastly, our operating cash flow and free cash flow was very strong. In fact, at $43 million, we generated more free cash flow in Q1 than we did all of last year. So we're very pleased with that start, and we think it's indicative of the cash flow generating opportunity we have with the Allscripts franchise. So now, let's look at a few of the highlights from each of these areas. Our first-quarter bookings, of the $236 million, approximately $150 million, or 63%, was derived from software delivery. This includes subscriptions, licensed software, hardware, and transaction-related revenue.

Please remember that maintenance associated with perpetual software licenses, as well as transaction fees that are not considered recurring, are not included in our bookings calculations, when we report them. The balance, or approximately 86% or 37% of overall bookings, came from the sales of our client service solutions. And this would include managed IT service contracts, as well as what we're calling other client services. Bookings were particularly soft in this last area of nonrecurring other client services. Again, this is primarily what we used to call professional services -- okay -- very project-oriented work.

As we had discussed on our fourth-quarter call, two factors continue to impact the volume and demand for these other client services. The first is a business model transition that is allowing us to offer a high value business proposition for new system sale opportunities, particularly for our Sunrise platform. We're going to market with a prescriptive and relatively predictable implementation methodology that utilizes a standard configuration set and incorporates proven and best practice clinical work flows. This allows us to complete implementations faster, and it wraps some of what used to be up-front, nonrecurring client service revenue into a recurring revenue service model for support and optimization services.

The second factor is the continued wind-down of regulatory demand for project-based services, which as of now has not really been replaced with new activities. Upgrades on projects, for now, are slow to come, or have been pushed out by these regulatory changes. Looking ahead at bookings, we're encouraged by the new client activity, and continue to be optimistic about our goal to grow bookings in 2015. And this is driven by the multiple factors that Paul covered, and I just mentioned above. However, the weakness in demand for low-margin hardware and project-based, nonrecurring other client services will impact our revenue outlook for the year, and I'll discuss that in a few moments.

We ended the quarter with total backlog at $3.5 billion, and this is a slight increase compared to the end of last year, as well as the end of the first quarter of 2014. Moving on to revenue. It's again a tale of two revenue types, growth in recurring revenues and declines in nonrecurring revenue. Total recurring revenue growth, again, was 3% on a year-over-year basis. But it's an even higher 4.4% growth, if you exclude support and maintenance.

I point this out simply because, as we've discussed many times in the past, we do not expect maintenance revenue to grow, due to the client preference for subscription-type models. Speaking of maintenance revenue, it remains very stable. It can vary from quarter to quarter, based on several factors, but our overall view remains for stable maintenance revenue for the balance of the year, in the range of $115 million to $120 million per quarter.

Moving to gross margins, performance this quarter was disappointing. Our total non-GAAP gross margins were 42.3%, and that was down 250 basis points from the year-ago period, and even 160 basis points from just Q4 of last year. The decline, though, in total gross margin is almost exclusively attributable to a decline in client services margin. During the first quarter, we elected to maintain our services staffing levels at a relatively consistent level with Q4, partly because we expected our New York-based clients to have to incur EPCS upgrades. That stands for electronic prescription of controlled substances.

We spoke a little about that on our last call. But we -- with our concentration of New York clients, we expected that there might be a lot of activity there. These requirements were subsequently delayed, and this contributed to the misalignment of revenues and costs, and it negatively impacted our overall margins. We are taking actions to reduce those costs in this area. And while we expect some improvements in client services margin from these actions in Q2, we would expect to return to more normalized margins on this revenue base in the second half of 2015, as we bring our services cost structure more in line with the revenue.

As I move to operating expenses, our non-GAAP SG&A declined approximately $11 million from the year-ago period, to $71 million. We have eliminated all nonrecurring-type expenses, except for severance, from our non-GAAP presentation this quarter. So specifically, in connection with the business realignment in the quarter, we did record severance charge of approximately $6 million. And this is excluded for purposes of calculating non-GAAP SG&A, non-GAAP operating income, and adjusted EBITDA.

While I do not anticipate other types of nonrecurring expenses, I do believe we will have additional severance charges in the second quarter, as we continue to adjust and align the business to meet our overall financial objectives. Our reported R&D for the quarter was $47 million, and we capitalized $9 million to our balance sheet. This yields a total gross R&D spend of $56 million, which is a $2 million increase from our fourth quarter. In total, while revenue and gross margins declined, operating efficiencies drove a 12% improvement in our non-GAAP operating profit for the quarter.

And our adjusted EBITDA, which you can find on table 5 of our press release, was $50 million, which represented a 15% adjusted EBITDA margin, also an improvement from a year-ago period. With regard to some other housekeeping items, we recorded approximately $3 million of non-cash interest expense on our convertible notes. This is the same as in prior quarters, and we continue to exclude this from our non-GAAP net income. Our non-GAAP net income totaled $15 million overall, and this equated to $0.08 per diluted share, which compared to $0.07 in the first-quarter period.

I'll wrap up my prepared comments by giving you an outlook for the rest of the year. As discussed, sales activity for project-based client services, as well as hardware sales, were weak during the quarter. And at this time, we don't see any significant catalyst to change that, so we believe it is prudent to adjust our outlook accordingly. As such, we're lowering our revenue guidance for the full year, to a range of $1.40 billion to $1.43 billion. However, given that this weakness is linked to very low margin, nonrecurring business, we do not expect it to have a significant bottom line impact.

And we are reaffirming our full-year adjusted EBITDA guidance of a range of $230 million to $250 million, as well as reaffirming our full-year non-GAAP EPS guidance of $0.42 to $0.50 per share. We would expect steady quarterly progression of revenue, adjusted EBITDA and non-GAAP EPS over the balance of the year. So with that, thanks for listening, and I'll now open it up for questions.

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

Your first question comes from the line of George Hill with Deutsche Bank.

George Hill - *Deutsche Bank - Analyst*

Hey, good afternoon, guys. Thanks for taking the questions. And thanks for the new presentation. I guess Rick, maybe, let's talk a little about the negative revenue revision. And like that the EBITDA revision is not changing. And I was trying to take notes as quick as I could. I guess was the net take-away here that you guys are going to be -- that the revenue that's rolling off is low margin? Or do you guys think you're going to be able to cut costs in line with the revenue shortfall to preserve profitability?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Yes, so George, it's mostly the first part of what you said. It's the revenue that we see softness in, is revenue that contributed very little to our initial plans, or EBITDA, that we would expect. But I would also point out that we are taking some cost actions, as well, namely in services area would be at the top of that list. But we've been continuing to try to run a more and more efficient operation, and that's not going to stop this quarter.

But services clearly sticks out. You can see we protected some resources in Q1, to make sure they were available, in the event we had to do upgrades. It turns out, we did not have to do those upgrades, and so we had a pretty good mismatch of cost and revenue. That -- we have to correct that mismatch, and we're doing that as we speak.

George Hill - *Deutsche Bank - Analyst*

Okay. And I guess with respect to the nonrecurring revenue, the business transformation is occurring in line with the way that you guys have prescribed, with the recurring revenue growing faster, and the nonrecurring revenue growing slower. Where do we think the nonrecurring revenue troughs that will help us from a modeling perspective?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

It's hard to call a trough, George. Obviously, the demand environment's pretty dynamic. But I will say we have -- when I look at our backlog right now, and I look at the revenue levels we experienced in Q1 for our nonrecurring areas, I -- in the near term, I have a hard time seeing it going much lower than it was this quarter.

George Hill - *Deutsche Bank - Analyst*

All right. Maybe if you'll let me just hop on one last one, Rick. Because you talked about the demand environment, I'll hit Paul with this one. Paul, some of the other vendors, in the quarter, have talked about either a lull in the market, or have had booking shortfalls. I guess from a macro market perspective, could you talk about the demand levels that Allscripts is seeing? Maybe a quick comment, both on the in-patient and the [in builds] for a segment? And I'll hop off.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

We had a pretty good ambulatory quarter. If you look at the results from our professional services business, our pro business, that we call our pro EHR, that actually had a pretty good quarter. Our global marketplace, while we didn't post a lot of scoreboard in there in Q1, was important to us. (inaudible) the fact that on the acute care side, we just signed Joint Township, another Sunrise win, is -- it also puts some wind in the sails for us, which is -- that's all very positive.

I also think, George, on the outsourcing, which I've been talking about for quite a while, there is a fair amount of activity in the outsourcing component. And there is also a fair amount of activity on the hosting component that we continue to take in, and have a lot of fruitful conversations with clients on. The other components that have been -- continue to show pretty good, robust strength, would be the population health, specifically the Care Management had a great quarter.

And that's the coordination care outside or above the EMR. And that, as you know, solution goes across anybody's solutions, so that we sell that a lot in the top 40 IDNs. That's a preferred solution to manage the post-acute coordination of care, outside the four walls of the hospital.

George Hill - *Deutsche Bank - Analyst*

Okay. Thanks.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thank you.

Operator

Your next question comes from the line of Sean Dodge with Jefferies.

Sean Dodge - *Jefferies & Company - Analyst*

Hi. Good afternoon. Thanks. Maybe starting with Paul. When you think about your long-term vision for the Company, what proportion of future revenue growth do you expect to be -- or maybe would you like to be -- driven by new client adds, versus cross-selling or up-selling into your existing base?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

I think when you incorporate the global part of the business, you would expect -- or I would hope -- that we have a larger percentage of new business than we have coming in today, given the amount of opportunity there is that not only in the US, for replacement marketplace, but also outside the United States. I'm not going to give a specific number, but I would like to have that number be clearly higher than what it is today. That will float all boats.

Obviously, our installed base is continuing to vote with their dollars, giving us additional dollars on a percentage of wallet share basis. But importantly, the new footprint, new accounts internally -- inside the US, as well as globally, are all big focus areas for us, where we have pretty good-sized force that's deployed globally, as well as domestically, to focus exclusively on new business acquisition for us.

Sean Dodge - *Jefferies & Company - Analyst*

Okay, and then -- thanks. And then maybe for Rick. You guys have made some good progress taking costs out of G&A, by reducing offices and management layers, over the past several quarters. Can you talk a little bit more specifically about what the focus is for the upcoming year? Is it going to be more of the same? Or are there other areas or inefficiencies you see, that you haven't addressed yet?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Yes, Shawn. We're -- I think this year we're -- and it's embedded in some of our guidance. We expect to work on some of our cost of sale areas, so some of our direct costs. That would include services, which now, as I pointed out, given the revenue falloff, has an even more acute need to do some fixing there.

But even beyond services, our support costs, our hosting cost, which is an opportunity we've talked about for some time, these are all focal point areas for us right now. But SG&A is a thing that -- we're embedding it in the culture of the Company right now, and it's a consistent crank on that. And so nothing radical, but we'll just continue to work on making ourselves more and more efficient there, as well.

Sean Dodge - *Jefferies & Company - Analyst*

Excellent. Thanks again.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thank you.

Operator

Thank you. Your next question comes from the line of Ricky Goldwasser with Morgan Stanley.

Zack Sopcak - *Morgan Stanley - Analyst*

Hey, this is Zack Sopcak for Ricky. I wanted to just ask first about the EBITDA guidance, and the growth for the rest of the year. So the growth is pretty substantial acceleration in the next three quarters. Could you talk a little bit about what drives you to the higher end and the lower end of that EBITDA guidance, over the next three quarters?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Yes, I think, Zack, the way -- the best way to think about is, look at -- just for high level math, look at what we've performed in the quarter, from an EBITDA basis. And as I said, we carried -- I don't want to label. We made a decision to protect resources, to make sure we didn't leave clients shorthanded, if they needed upgrades. But in hindsight, you look at it, we had unnecessary costs in the quarter. That's not an insignificant amount.

So I would say if you took our reported results, pro forma-ed them for that cross layer, that gives you a sense of what our run rate is. And you take that, and then add some of the revenue growth that we're projecting off of this quarterly number, remember. This is pretty low quarterly revenue, too. So lift the revenue, take profitability off of that, and add that to a pro forma run rate. And I think you'll find yourself around the range we're talking about.

Zack Sopcak - *Morgan Stanley - Analyst*

Got you. Thank you. And just to follow up on that expense that you talked about, for the EPCS. Maybe it's a little early, but when you think about that being delayed until 2016, are you thinking, again, that would you be ramping up for that, as well, as you get into 2016? Or is it, you'll wait closer to that time to make that determination?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Our services team is working hard to build a more predictable and efficient model. I don't want to get too longwinded here. But it's important they create -- we have a base load of resources, that for base level demand. And then we can flex up the resources, when demand flexes up. And that's the kind of operating model we're put putting in right now, and our leadership team in that area is working hard to implement that.

Zack Sopcak - *Morgan Stanley - Analyst*

Okay. Great.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

So we shouldn't -- we should try to avoid some of these mismatches in the future.

Zack Sopcak - *Morgan Stanley - Analyst*

Great. Thank you.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

You're welcome.

Operator

Your next question comes from the line of Gavin Weiss with JPMorgan.

Gavin Weiss - *JPMorgan - Analyst*

Thanks. I just wanted to touch base on the -- I think it was the Grand Lakes win in Ohio. You talked about it being a competitive process, and the product that helped you win that deal. I just wanted to get more color on what you really thought was the most important factor? And was it something that maybe you wouldn't have been able to win two, three years ago? And lastly, just wanted to confirm that it was signed in the second quarter, included in 2Q bookings, not 1Q.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

It was a 2Q transaction, so that is confirmed. I would say that, Gavin, this was a pretty interesting relationship that we just created. They're pretty interested in having a predictable model, where we have a fixed fee relationship with them, over the time of -- over an eight-year period of time. They are interested in the all-in model, so it's revenue cycle. It's the new functionality that we've come out with for our emergency room, ambulatory, all on a single platform.

And to answer your question, is this something that we could have competed successfully for a couple years ago? I think not. I think the R&D spending that we placed, appropriately, in the Sunrise environment, over the course of the last 2 1/2 years, has been paying some dividends. Not only with our existing clients, but with some new client wins like this. Where you have an integrated inpatient, outpatient revenue cycle and a population health component, where they can grow into that, or they can put it in place day one.

Gavin Weiss - *JPMorgan - Analyst*

Okay. That's helpful. And I think, Paul, you had mentioned -- there was a fair amount of activity on the remote hosting side. And Rick, you've talked about this as being one of the opportunities to improve margins this year, from your new remote hosting agreement. And I just wanted to get an update on your expectations for that business in 2015?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Yes. So hosting, again, let me just start by -- our new presentation format is part of our managed IT services. Right? It's a recurring-type business, so it's in that area. In terms of your specific question on performance, yes, the -- it's a big focal point for us. There's a couple of factors that help improve profitability. Some of it comes from scale. And we do turn live, or expect to turn live, a fairly significant deal that we sold late last year.

That should come live early in Q3. That will help create some scale benefits, and leverage fixed costs a little better. But we're also, as you indicated, renegotiating some of our third-party contracts. We expect to have those finished this quarter. And so we'll start to accrue some benefits from that, as well. And all in all, our goal remains to get that remote hosting business area to a breakeven or better level, by the end of this year.

Gavin Weiss - *JPMorgan - Analyst*

Okay. Great. Appreciate the comments. Thank you.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thank you.

Operator

Your next question comes from the line of Sandy Draper with SunTrust.

Sandy Draper - *SunTrust Robinson Humphrey - Analyst*

Thanks very much. Maybe just a follow-up to an earlier question or comment. Do you know -- my understanding is that sometime, by the end of this year, you may have one or two sites that are essentially running close to the full suite of products, both on the inpatient side for Sunrise, so rev cycle, clinicals, et cetera. Is that true? Do you think you're going to get there? Or do you already actually have somebody that is running the full suite? Thanks.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

We've got a couple clients that are very close to having that full suite. We've got a couple clients that are putting in the new version of Sunrise Financial Manager. That would complete that, Sandy. We've got some people that are running an older version of it, called Patient Financial Manager, so we've actually got revenue cycle systems sourced through us.

It does not happen to be the Sunrise financial manager. We've got another client that has that running in Texas, so the number of two to three is a good standard to go by. And organizations that are getting a fair amount of benefit out of that, and proving the value of the total integrated platform from Allscripts.

Sandy Draper - *SunTrust Robinson Humphrey - Analyst*

Okay, that's helpful. So would it be safe to say, by the end of the year, you would be targeting to have a couple of sites, that are reference-able, that are all on the new platform? Or is that really something that might happen in 2016?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

By the end of the year, that's a good -- that would be -- that should be done.

Sandy Draper - *SunTrust Robinson Humphrey - Analyst*

Okay. Great. That was my question. Thanks.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thank you.

Operator

Your next question comes from the line of Charles Rhyee with Cowen & Company.

Charles Rhyee - *Cowen and Company - Analyst*

Yes, thanks for taking the question. Paul or Rick, I think in the past, you talked about Sunrise Financial Manager -- maybe I think it was the HIMMS meeting or the last quarter call -- that that was an area you still needed to do some work. Can you talk about the progress in improving that platform for clients? Particularly as related to the earlier question here, you're going to have a lot of clients -- several clients running the full suite? Thanks.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Yes. I think the -- we somewhat discussed it in a minute ago, but the progress there has been very good. We've had a lot of folks that have been giving us -- the early adopters have been giving us a lot of very important feedback. Not only on the actual functionality itself, but the work flows. The work flows circa 2015 are different than the work flows that somebody might have been doing when some of these systems were built 20 and 30 years ago. Specifically around the advanced payment plans that are out there, the accountable care organization, payment systems.

How you process claims differently on -- and what kind of information you collect on the front end. The self-pay components to it. There's a whole bunch of different types of processes that an accounting person, inside the four walls of a hospital, and importantly in a clinic, go through today that didn't exist 5 and 10 years ago, or even 30 years ago, when some of these systems were originally contemplated. So the workflow component of this, we think, is pretty exciting, and it's going to be different. And that's why we're pleased with the feedback we're getting from clients. But importantly, that the input is being directly coded, and put into process, and put in production.

Charles Rhyee - *Cowen and Company - Analyst*

If most clients are not running at a full -- not everybody's in an ACO, not everyone's doing -- clearly, nobody's doing 100% at-risk contracting. How much of this is really being demanded, though, at the moment, by your clients?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

I think if you ask the client, almost every client has some form of an at risk payment. Whether that's the new government Medicare, Medicaid work that's going on, and some of the new legislation there, that will be a component of reporting on the quality, and then getting reimbursed for that. The -- and depending upon what part of the country you're in. So in California, I think they would beg to differ a bit. I think they're mostly at full cap in California, depending upon, again, the type of client. Like most of our ambulatory clients in California have been on a full cap contract for a very long period of time.

So I think when you build a system like that, it has to incorporate all different types of clients, and all different states across the US. And then, of course, outside the United States. So it's pretty complex. But the flexibility that we have, with the way that we've designed the work flows, we think will enable us to be in a much more competitive position, on a going forward basis. And we see a fair amount of demand coming our way, because of people that will be subjected to the new billing processes looking for a different system.

Charles Rhyee - *Cowen and Company - Analyst*

And when do you expect that to be available -- generally available, you'd say, with this in place?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

I think by the end of this year, we'll have -- we already have clients that are in production today. But by the end of this year, we'll have, as I said, two to three more.

Charles Rhyee - *Cowen and Company - Analyst*

Okay. Great. Thank you.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thanks, George.

Operator

(Operator Instructions)

Your next question comes from the line of Robert Jones with Goldman Sachs.

Adam Noble - *Goldman Sachs - Analyst*

Thanks for the question. This is Adam Noble in for Bob. Just thinking about the bookings, I was wondering if you could assure if there were any unusually large wins in there? Or whether this is just a much broader base of bookings wins? And thinking about the two hospital wins in the quarter, anything you could share around your relationship with those clients before, on the ambulatory side, or with any other products?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

So maybe we'll take them in reverse order. The two hospitals that Paul talked about, we -- one was actually first quarter, and one second quarter, in terms of signing those contracts. So we're talking about them both now, but Palo Verde was -- came in just at the end of the quarter. No relationship prior to these opportunities. So that's a -- those are new footprints, and we're very thrilled to have them in our client portfolio now. In terms of, was there anything unusual in the bookings for the quarter? Nothing unusual, per se.

We've had a couple of -- every quarter looks slightly different. But we are trending a little bit more towards larger deals, as we get -- particularly as we get some of our new sales team extending our Sunrise footprint. So we do that, and we're still -- we're really seeing some really good traction in our payer life science area. So extending our platform or network and information to the provider universe, and pharma universe, is proving to be a good business opportunity for us, as well. So those are areas that are strong. But I wouldn't say there was anything unusual, beyond that.

Adam Noble - *Goldman Sachs - Analyst*

Okay. That's really helpful. And just to sneak one more in. Given the 1Q shortfall in revenue, even with revised guidance, still implies a pretty healthy increase from 1Q levels. Should we expect the growth to come primarily from subscriptions and managed services? And would you expect the rest of the segments to at least hold 1Q levels for the remainder of the year?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Adam, I'd refer to a little question I talk -- a question I answered a while ago, which was -- I think George asked it. But it was about whether we had a trough or not, on some of the nonrecurring stuff. And I -- it's hard to label it. It's hard for me to label it exactly that way. But I would expect given where we started, that there will be some upside from some of those nonrecurring areas. But I think we're on a nice, steady diet of increases in recurring business, and that's what we'd expect to continue, going forward.

Adam Noble - *Goldman Sachs - Analyst*

Thanks so much.

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

You're welcome.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thank you.

Operator

Your next question comes from the line of Jeff Garro with William Blair & Company.

Jeff Garro - *William Blair & Company - Analyst*

Good afternoon, guys. Thanks for taking the questions. With the two Sunrise wins, I wanted to check in on the expectation that you set last quarter, of roughly 1,500 hospitals coming to market in 2015. I want to see if this is still the right expectation for replacement activity? And whether a proportional amount, you think, has surfaced within the first four months of the year?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Yes, I said -- I was quoting some information that came from KLAS on that 1,500. I do think that there's a fair amount of activity in the marketplace. We have our quarterly forecast meeting, where we bring everybody in, and we bring the new business guys in, and they talk to us about the deals they're working on, both domestically and globally.

And I do still feel that there is a fair number of clients that we're seeing, that we're talking to, that are prospects, that are in the process right now of making a decision. And the rate at which those have come thus far, we'd like to some -- to see them actually make decisions more quickly, and more of them come. But we have a fair number of folks that are out there today that are -- where we have been selected, or we have been down-selected to a couple, where it's still competitive, but we like our odds there.

Jeff Garro - *William Blair & Company - Analyst*

Great. Thanks. And then one more question. Just curious on how you see the addressable market within your own client base for that outsourced RCM service? And what your game plan is, to capture a good chunk of that opportunity?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

It's a very important market for us. We have such a large number of ambulatory physician office practices. And those folks are very intrigued by an offering, not only to allow them to capture more revenue, and be more robust in that respect. But also to participate more heavily in the ecosystem around the accountable care organizations, where we can help them build a clinically integrated network.

Or we can help them build a set of contracting services, where they can actually learn how, and participate in, at-risk contracts. And then the last thing is, we actually can provide some, if you will, lower cost per unit scale for them, to be their back office IT infrastructure, for the things like Analytics, dbMotion, FollowMyHealth, and being able to host that for them. So that's a -- we've been very pleased with the original interest level. And in some of the pieces that I've talked about, we've already signed a number of new contracts.

Jeff Garro - *William Blair & Company - Analyst*

Great. Thanks for taking the questions, guys.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

You bet.

Operator

Your next question comes from the line of Eric Percher with Barclays.

David Ho - *Barclays Capital - Analyst*

Hi, good afternoon. This is David Ho on for Eric today. I wanted to ask about the bookings. Can you talk about whether the level of bookings that are recurring, is that in line, or higher or lower than it has in the past? Just trying to get my footing around it, given how it's been changed in the presentation?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

So David, if you look at the supplemental data that we provided, we actually give you, I think, a pretty good split on how those bookings align with our services, versus more what we would call the software-related. So it gives you, I think, a pretty good look of the current quarter, and how that compares to prior quarters. We did skew a lot higher, this quarter, towards software -- what we call software delivery. Which again, software delivery is all of our subscription software, licensed software, any transaction-related revenue, and any hardware, would all be up in software delivery.

And conversely, all the services are accompanied in client services. So weakness, in nonrecurring services in particular, is what is bringing down client services, relative to what you've probably seen in prior quarters. And we offset that with some pretty good strength in the software area during the quarter. So that's why we -- in part why we've given the new presentation, is to help give a little more transparency on those type of things.

David Ho - *Barclays Capital - Analyst*

Okay. And my next question is just broadly around Meaningful Use stage 3. I was wondering what you guys think about the draft rules? And particularly, if requirements for patient portals are replaced with APIs, how does that -- how will that affect the current FollowMyHealth client base?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

I think the current FollowMyHealth client base has somewhat pivoted to a consumer engagement platform. So what I think people have noticed, in the fact that they've got a lot of patients already utilizing the system, is that it's not just something -- or a medium by which the organization can communicate with the patient. But it's also a medium by which the patient is communicating with the organizations. And so it's somewhat flipped from being some -- a patient engagement to being a consumer-driven initiative.

And I think there's going to be a lot of people, that have access to healthcare, that are going to use their portal much more robustly. Especially when they go on their portal, and they're able to see not only that institution's data, but also data from other institutions that have -- that they have visited, as a result of our non-tethered approach, and our architecture, which is different than most of the other portals that are out there. So I see that we're very much in line with a lot of what the MU3 guidelines are asking for, and what the patient engagement and consumer components are.

Given not only cost, quality and other information, but the transparency of the data that the people are going to be able to use, not only about their own health, but as they're looking for care and provider organizations around town, based on quality, based on cost, and based on convenience. So I look at that as being an extraordinarily important and robust platform for us. We have, inside of that organization today, as we look at the number of people that are utilizing it, we have over 3,154 facilities that have our FollowMyHealth information coming out of, and going into, the FollowMyHealth portal.

We have over 339,000 providers that have accessed the portal. And we have 4.3 million patients that not just -- or that we can see -- but are -- that have actively, and are actively, working with data that are inside of their portal. We can see millions more than that 4.4 million. But these are people that are actively using it, that are accessing it daily or weekly, have a fitbit attached to it, and are utilizing that to really manage their or their family's health.

David Ho - *Barclays Capital - Analyst*

Thanks for the detail.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

You bet.

Operator

Your next question comes from the line of Michael Cherny with Evercore ISI.

Michael Cherny - *Evercore ISI - Analyst*

Evening, gentlemen.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Michael.

Michael Cherny - *Evercore ISI - Analyst*

So I wanted to dive in a bit. I think a bunch of us on the line here spend plenty of time at HIMMS walking around the floor, hearing about all the different approaches towards population health management. You guys have obviously taken a very distinct approach that has shown some tremendous measures of success.

As you think about the way you approach the population health management market, and particularly, also, in conjunction with the improvement you've seen on the cash flow side. How do you think about the deployment of capital on that front? Both from a R&D perspective, as also -- as well as potentially looking for additional bolt-on acquisitions, that might make sense to add on to what you already currently have?

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Yes. I think, Mike, just as a starting point, obviously, population health is on every healthcare provider's mind right now. And we think that trend will grow, not shrink. So from our perspective, it's important to continue to invest in evolving the solutions we have. We feel really good about our head start in the space. Integrating some of those solutions together is another high priority of ours. And then we will look to augment the capabilities we have today.

Analytics is obviously an area that everybody's talking about, and everybody needs go to. And we believe that's a capability we're investing in already, and it's an area we'll continue to invest in. So that's definitely an area that is high on our list of areas to invest in. Whether it's purely an acquisition, though, is a different question. And I don't have to tell you that some of the folks that are -- or companies that are out there, fairly immature companies, are with advertised capabilities, are trading at crazy valuations.

And we've looked at a bunch, and we will continue to look at a bunch. But right now, we have a pretty good plan that is not heavily dependent on acquisitions.

Michael Cherny - *Evercore ISI - Analyst*

Thanks. That's helpful.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thanks for the question.

Operator

Your next question comes from the line of David Larsen with Leerink Partners.

David Larsen - *Leerink Partners - Analyst*

Hey, guys, congratulations on a good quarter, and good bookings growth.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thanks, David.

David Larsen - *Leerink Partners - Analyst*

Sure. Can you maybe just talk a little bit about professional services bookings? Like I think last quarter, maybe they were down a bit, year over year. Did those come back this quarter? Or would those be included in client services? And maybe what is driving that trend? Thanks.

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Yes. So David, they're in the category of client services. But I'll point out again, on our supplemental data sheet that we created, we actually drill down into client services a bit. And we try to distinguish what we'd call recurring services from nonrecurring. And so traditionally, what we talked about was professional services, which was nonrecurring, project-based work, is now all in the other client services line, in that area.

The bookings -- which you don't quite see at that level of detail, but you can see in aggregate. The bookings for client services were softer during the quarter, and that area, in particular, as I made reference to in my comments, was a weak area of demand for us this quarter. And that's, again, a large part of why we're modifying our revenue outlook for the year. I talked a lot -- or I tried to address some of the trends that are happening there, David. We also talked about on our fourth-quarter call. But it's a combination of what we -- we have created a much more efficient implementation methodology.

So where we used to have to charge a lot more for services activities, that's been crowded -- and that crowded out dollars that could be allocated to software or other higher-value service areas, we've now done a lot more efficiently. And so the result of that is, we're much more competitive in the market, but we have lower services coming off of that, or lower -- what we're calling other client services. So that's one trend. We're also seeing clients coming off of regulatory requirements and now staring at ICD-10. There's a lot less upgrade activity happening in the market right now.

David Larsen - *Leerink Partners - Analyst*

Okay, that's very helpful. And just one more follow-on, if I can. Do you think this $47 million or so is a pretty good run rate, as we head into 1Q 2015? Have you streamlined this more efficient, more cost-effective process? And maybe we'll see a bump for ICD 10s, as we approach 3Q of 2015? And then also, were your ambulatory bookings up, year over year, for TouchWorks in particular? Thanks.

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

You had a lot of questions in there, David. So you may have to go over that again. Your starting question was, is --

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David Larsen - *Leerink Partners - Analyst*

Are the professional services -- have they stabilized, on a quarterly basis, do you think?

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Yes. So I would say at $47 million, as you said, which is really what is other client services revenue, I would say we've gotten a couple of different variants of the same question, which is, are we troughed or not on that area? I believe our nonrecurring revenue was pretty low in the quarter, and my expectation is that's -- won't -- in the near term, this is not going to go any lower than that.

So I guess another way of saying that I is, I would hope that -- I would expect that to rise. But I could look at that a little more, not so much about the services, but as I do comment on the nonrecurring system sales, as well. So in totality, nonrecurring should rise from where it is. Services, probably a little less apt to rise than where it is right now.

David Larsen - *Leerink Partners - Analyst*

Thanks a lot.

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

So that's part one. I don't know if there was a second part to the question.

David Larsen - *Leerink Partners - Analyst*

Your ambulatory bookings, were those up in the quarter? Thanks.

Rick Poulton - *Allscripts Healthcare Solutions Inc - CFO*

Ambulatory bookings were up and strong during the quarter. And we expect continued strength in that area.

David Larsen - *Leerink Partners - Analyst*

Terrific. Thank you.

Operator

Thank you. At this time, there are no further questions. I would like to turn the call back over to Paul for any closing remarks.

Paul Black - *Allscripts Healthcare Solutions Inc - President and CEO*

Thank you, for everyone, for joining the call today. To summarize, we're very pleased with Allscripts' position in the market. We continue to focus on areas that require attention, while investing in high-margin recurring growth opportunities, to support the Company's client base and our full-year projections. The evolution away from payment for volume, and towards payment for value, can and will be disruptive, and concerning to providers that historically have been rewarded for delivering more services on a fee-for-service basis.

Value-based payment creates both incentives and data transparency opportunities, and enhances the quality and cost efficiencies that could be achieved through the integration of these solutions for patients, communities, payers and providers. And in that arena, we feel very confident in Allscripts' ability to lead the healthcare industry during this transformation. Thank you very much for your calls -- your time tonight, and good night.

Operator

Thank you. Ladies and gentlemen, that does conclude the conference call for today. You may now disconnect your lines.