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MDRX - Q3 2015 Allscripts Healthcare Solutions Inc Earnings Call

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OVERVIEW:

Co. reported 3Q15 total revenues of $355m and non-GAAP net income of $25m or $0.13 per diluted share. Expects full-year 2015 revenues to be $1.390-1.405b and non-GAAP EPS to be $0.45-0.47.

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PRESENTATION

Operator

Good afternoon. My name is Amanda and I will be your conference operator today. At this time, I would like to welcome everyone to the Allscripts third-quarter 2015 earnings conference call.

(Operator Instructions)

This call will last approximately one hour. Thank you. I would now like to turn the call over to Mr. Seth Frank, the Vice President of Investor Relations. Please go ahead.

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

Thank you, Amanda. Good afternoon. Our speakers today are Paul Black, Allscripts' Chief Executive Officer, and Rick Poulton, Allscripts' President and Chief Financial Officer.

A few opening forward-looking statements here. Some of the statements we will make today will 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 actual results to differ materially. 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 SEC filings for more detailed descriptions of the risk factors that may affect our results.

Now I would like to turn the call over to Paul.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

Thanks, Seth. Welcome to the Allscripts third quarter earnings call. Results this quarter were strong across the business. Bookings of $272 million were a third-quarter record and the third consecutive quarterly record this year.

Recurring revenue is strong and continues to climb. Gross margins increased for a second quarter in a row. And continued focus on containing operating expenses drove double-digit growth and adjusted EBITDA and non-GAAP EPS. Quarterly new client count is approximately 180, and totals 560 year to date. Overall, this quarter demonstrates excellent momentum in the business globally.

Now some details. We had a great quarter in the Sunrise platform, driven both by new clients and add-on sales to our existing base. We signed University Hospital of South Manchester, an 850-bed teaching hospital in Manchester, England, to the Sunrise platform. This client will implement a complete solution including Sunrise Acute and Critical Care, ED, Mobile, FollowMyHealth and Patient Flow.

State-side we won a highly competitive opportunity with Baptist Healthcare in Pensacola, Florida. Baptist is the largest new Sunrise agreement in the United States market in recent years. It includes Baptist hospital, a 492-bed tertiary care facility, two additional hospitals, several medical parks, and associated physician practices, including the prestigious Andrews Institute for Orthopedics and Sports Medicine.

Baptist is going all in with Sunrise as an integrated platform for inpatient, outpatient, and revenue cycle management across all care settings. This includes Allscripts population health solutions including dbMotion, FollowMyHealth and EPSi.

The success we're having in the acute replacement market is a function of strong clinical functionality, a compelling total cost of ownership model, and an implementation approach that is highly efficient. We believe the wins this quarter firmly put to bed the myth that there are only two competitive alternatives in the marketplace.

In the physician market, bookings were strong as we grew both our EMR footprint and recurring managed services. We are expanding Allscripts with Catholic Health Initiatives, a strategic long-term TouchWorks client. CHI has engaged Allscripts to manage the daily requirements of its mission-critical IT infrastructure and clinical operations. This approach allows CHI to focus on delivering outstanding patient care.

This week another one of our largest Allscripts TouchWorks EHR clients, Advocate Medical Group, selected Allscripts hosing solutions to help improve system stability and overall performance. Advocate also signed a long-term extension for TouchWorks.

Successful implementations at Southern Illinois University where 400 providers went live in one day, highlighting TouchWorks' scalability and large multi-specialty groups. Capital Care Medical Group, a 130-provider multi-specialty group practice in Albany, New York, chose Allscripts Practice Management and Payerpath solutions as a replacement for its legacy practice management solution. They also extended their TouchWorks EHR term for seven years.

New client bookings for Professional EHR and Practice Management were strong in Q3. New provider counts are at the highest level in several years.

A key to our success in the EHR market is Allscripts' approach to designing solutions based on client feedback and the use of best-in-class UI design processes. I am proud to announce Allscripts received a perfect score for TouchWorks and Sunrise on a recent comparison of EHR vendor user-centered design processes, usability testing methodology and transparency of test findings. The scoring was on a valuation framework created jointly by MedStar Health, National Center for Human Factors in Healthcare, and the American Medical Association.

The framework was based on best practices and recommendations from the human factors and usability literature and on the ONC's user-centered design criteria. In addition to strong usability testing methodology, these perfect scores reflect the rigor Allscripts applies to our entire user-centered design process as we research and design solutions with usability and safety in mind.

With the multi-year investments that we've made in our core EMR solutions we are seeing success in retaining and in attracting new clients for managed services, our value-based care program and RCM services. We see demand by healthcare providers to migrate to value-based care, create ACOs, conduct patient outreach, and utilize analytics for care improvement and cost management.

A first step in this journey is implementing chronic care management programs, allowing for improved care quality and outcomes for the chronically ill populations. We have signed up dozens of clients representing hundreds of physicians. We have enrolled tens of thousands of patients in value-based management programs that will generate improved patient care and revenue opportunity for our clients. The ACO service offerings complement Allscripts' leadership in solutions for population health management.

A large west coast health plan contracted with us for dbMotion to manage the care-specific patient cohorts. We added multiple second-generation consumer engagement platform clients in Q3, including Catholic Health Initiatives who will replace a legacy third-party portal with FollowMyHealth across its 1,500 TouchWorks providers. This is the largest FollowMyHealth contract that we've ever signed.

We see good demand for post-acute and transitions of care solutions, reflecting attempts to aggressively manage acute care utilization. New client sales were strong for other population health solutions such as Homecare and EPSi. The largest not-for-profit hospice in Illinois selected Homecare in a highly competitive situation. A major south Florida health system chose Homecare over an integrated module available from its incumbent EHR supplier. A children's hospital in northern California selected EPSi for cost accounting over competitive solutions and its legacy solution provider.

Our global business continues to pick up momentum. Allscripts' investments in these markets continue to produce results of client satisfaction and new business. New client go-lives have been successful, such as the Guam Regional Medical Center, with an integrated Sunrise clinical and revenue cycle solution during Q3.

We continue to have renewals and extensions across global markets. For example, the provincial government in Canada will extend Sunrise as their ehealth foundation across the entire jurisdiction. Accomplishing early outcomes with their strategy, they continue to advance our solutions across the continuum, while focusing on improving access to care - a provincial priority. This province is also at the forefront of connecting the community by leveraging our population health platform, dbMotion, to connect over 420 primary care clinics.

Looking at Allscripts' strategic priorities in the market, we continue to focus on leadership and innovation promoting open interoperable systems. We have led in this area for many years, and now healthcare leaders are seeking interoperable solutions to overcome data silos and data blocking attempts across disparate EHR systems.

When HIEs are unavailable or not practical we have seen a tremendous uptick in clients sharing data via Allscripts Direct, a format physicians can use to send summary of care information without interface or middle layer of technology. Where HIEs are available clients are sharing data bidirectionally with either state or regional HIEs, allowing them improved access to clinical information. And for organizations who want to minimize clicks to impact, dbMotion enables highly sophisticated open systems to connect our semantic interoperability platform to normalize and share data, delivering it directly to the clinician's work flow.

Today dbMotion connects over 808 distinct source systems to more than 640 hospitals and healthcare facilities around the globe. One national health system client is receiving an average of 3 million messages a day, and in one month added almost 800,000 new encounters across the dbMotion platform.

In Q3 we completed an implementation of dbMotion across a major health system in the southwest. Since the initial rollout in March, the platform has successfully processed more than 36 million messages and connected more than 1 million patients. 14 different source EHRs are connected, emblematic of most US healthcare markets, as they manage care across complex settings through multiple EHRs in their communities. This client plans to aggregate data from 18 different source systems across more than 90 facilities, including an associated care organization and six different health plans.

Allscripts' success with consumer engagement has been remarkable over the last three years. In southern Illinois, Memorial Physician Services has achieved 17% of the group's patients, almost 19,000 people using FollowMyHealth. In fact, all major providers in the Springfield area are utilizing FollowMyHealth, providing patients with a single consumer record sitting on top of multiple electronic medical records, eight major hospital and clinic organizations in southern Illinois.

Here's a few statistics on FollowMyHealth. We're connected to over 8,775,000 patients, 1 million of whom are attached to two dozen organizations, demonstrating the use of a portal, which is what we call non-tethered. In other words, it can connect to multiple different electronic medical records. They don't have to be all sourced from Allscripts. We have over 3,522 different organizations who have access and are attached to FollowMyHealth. And we have over 399,000 providers who are also attached and using FollowMyHealth to connect and to communicate with their patients.

To conclude, I'm very pleased with our Q3 performance. We are improving EHR systems globally, installing interoperable and open solutions and facilitating better transitions of care. We are adding hundreds of thousands of patients and providers to our consumer engagement platform. Longer term we see the opportunities for paradigm shifts in care, utilizing precision medicine through genomic technology that will change the way healthcare and wellness are being managed.

Now I will turn the call over to Rick.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Okay, thanks, Paul. And good afternoon, everybody. Thanks again for joining us today. As I review the third-quarter details, please reference both our GAAP financial statements as well as the non-GAAP tables in our earnings release and the supplemental data book that's posted to our Investor Relations website.

To reemphasize some of Paul's opening commentary, the third quarter was a strong one for Allscripts on many fronts but particularly in terms of financial performance. Results continue to track well against our annual guidance, and the overall picture nine months into the year aligns with what we've been saying to you for multiple quarters about our goals -- specifically, annual growth in bookings, an increasing mix of recurring revenue as a percentage of the total, improving gross margins, continued operating expense control, and all of which collectively yield significant double-digit growth and adjusted EBITDA earnings per share and cash flow.

So, we remain very focused on delivering on the commitments we have made to both our clients and our shareholders. And our execution across the Company has never been stronger than it is right now.

Let's look at sales. Once again, we recorded $272 million of total bookings. This was a third-quarter record, and it's the second highest bookings level in Allscripts history. From a growth perspective, bookings increased 22% versus last year's third quarter and were up 13% on a year-to-date basis.

From a mix perspective, approximately $120 million, or 44% of the total was related to software delivery. These software delivery bookings increased 4% in the quarter and 12% year to date. Recall that software delivery includes our subscriptions, licensed software, hardware, and transaction related revenue. And, once again as a reminder, maintenance associated with perpetual software licenses is not included in our bookings metric.

The remaining $152 million or 56% of the total bookings were related to client services. These include both recurring services such as managed IT, rev cycle management, and value-based care services, but also include non-recurring other project-based client services.

Paul highlighted a few of the notable transactions in the quarter that contributed to these results. And that includes both our new Sunrise wins at both South Manchester as well as Baptist Pensacola, and also the managed IT services agreement that we signed with Catholic Health. But we really saw widespread strength across inpatient, ambulatory, and post-acute market segments. It's important to note that the Sunrise wins have a significant services content in those contracts, so those transactions get split across the mix categories that I discussed above.

As a result of our sales activity for the quarter our contract backlog was $3.6 billion at the end of the quarter. This is a 4% increase year over year, and it's up $150 million from last year's third quarter.

Transitioning over to the P&L, our total revenue increased to $355 million in Q3, a 2% overall increase on a year-over-year basis. However, in terms of revenue mix we again saw similar a trend to what we have seen all year, with stronger growth in our recurring revenue, which has been significantly offset by declines in our nonrecurring revenue.

But the rate of decline for nonrecurring revenue has slowed and this allowed us to realize a new overall growth for the first time in the last four quarters. So, we're quite pleased with that.

Recurring revenue, which consists of our subscriptions, recurring transactions, support, and maintenance, as well as recurring managed services, grew 6% on a year-over-year basis and it constituted 75% of our total revenue. This is up 300 basis points from the third quarter of last year. Also, just for perspective, excluding support and maintenance revenue, which, as we have discussed in the past, we do not expect to grow much due to an increase in client preference for subscription-based models, our recurring revenue increased 12% on a year-over-year basis.

Our recurring managed services revenue was a standout with 20% growth year over year, driven by the areas Paul discussed, specifically hosting, outsourcing, value-based care services, as well as revenue cycle. Our non recurring revenue was down 9% year over year, but essentially flat on a sequential basis with Q2. As I reflect on the last four quarters as well as what we see in backlog today, I would expect nonrecurring revenue to continue to be in the $80 million to 90 million range quarterly for the near term. So, we should be near the end of anniversarying large year-over-year declines.

As I look ahead to Q4, similar to last year I would expect project-based services work to be a little lighter than we saw in Q3 due to the holiday season. So, overall, this may take us a little closer to the middle of the range for nonrecurring revenue. On a long-term basis we'll continue to emphasize recurring revenue and our new sales activity. And we'll do that in order to help provide more predictability and buffer what modest volatility we see in the nonrecurring buckets.

Turning to non-GAAP gross margins, as we've discussed in both our first- and second-quarter earnings conference calls, we expected to see significant improvement and we were very pleased with the 46.4% margin that we realized this quarter. Margins improved both across our software delivery as well as client services. Within software delivery, where we posted our highest margin ever at 64.5%, we benefited from both favorable mix of our own software versus third-party software or hardware. And we also benefited from improved support in maintenance margins.

So, while mix can change quarter to quarter we believe the support margins are durable. Looking ahead we expect to continue to post better than historical average margins in this area.

Within our client services, prior actions taken to align our resources with client demand, as well as improving our hosting margins, helped us reach our goal that I discussed at length in our second-quarter call of achieving low double-digit levels by the fourth quarter of this year. So, we're very pleased to have achieved this result one quarter earlier than we had planned and to have done it so decisively.

Moving down to operating expenses, Allscripts non-GAAP SG&A declined 4% from the year-ago period to $76 million. We saw a small uptick in SG&A on a non-GAAP basis compared to Q2. This is not due to an increase in core spending but rather it's a seasonal effect from our ACE user group conference that we hosted in August. And I had previewed in that our last quarter's call as an anticipated event. As a result I would expect slightly lower SG&A in Q4.

You will note on table 4 of the press release, which contains our non-GAAP income statement, that we recorded $9.9 million of nonrecurring expenses in Q3. And that's larger than the $2 million to $3 million that I discussed last quarter. While we had a modest amount of charges in the quarter for severance and work efforts surrounding the DoD proposal, and those were in line with what I had forecast last quarter, the balance of this charge relates to the settlement of some outstanding litigation.

Removing litigation risk overhang has been a theme for the Company all year. And while we would, of course, prefer not to have this one-time expense, we believe that our efforts in Q2 and Q3 removes significant uncertainty surrounding potential future litigation liabilities for the Company. So, all in all we think it was well worth doing.

Looking at R&D, we recorded a total expense of $48 million on the income statement, and we capitalized $11 million to our balance sheet. Thus our total gross R&D spend was approximately $59 million for the quarter, and that's a 5% increase year over year. We maintain a strong commitment to innovation for our clients in building out our capabilities in emerging areas of healthcare. And we will continue to do this while still generating significant increases in profitability and cash flow. Same theme that we discussed last quarter.

Moving down the P&L, our adjusted EBITDA, as calculated and illustrated on table 5 of the press release, was $66 million, a 44% increase year over year and a 540 basis point improvement in margin on a year-over-year basis. This is a great performance, and it's emblematic of the leverage that we have in our business.

Accounting rules required us for GAAP purposes to apply equity accounting methods to our investment in NantHealth. This resulted in a non cash pretax reduction of $1.4 million to GAAP pretax earnings in the quarter. We expect to have similar accounting treatment until NantHealth converts from an LLC to a C corp, and then at that time we would expect to revert back to a more traditional cost base method of accounting. So, for now, while we have this accounting effect, this amount is added back for purposes of calculating adjusted EBITDA, non-GAAP net income, as well as non-GAAP earnings per share.

In terms of interest expense, as is typical, we recorded approximately $2.8 million of non cash interest expense. That's related to our convertible notes. And we continue to exclude those from non-GAAP net income.

As discussed in our press release we amended our bank credit facility during the quarter. This provides us with numerous benefits including an increase of $150 million in availability. It also provides lower drawn pricing. It provides us significant covenant flexibility, and also extended the tenor of the facility. All in all, this new facility will provide us significant strategic flexibility as we look ahead.

But as a result of this amendment, we had to write off $1.4 million of previously deferred debt issuance costs. This is included in our GAAP interest expense for the quarter but we do exclude this for non-GAAP results.

Finally, our non-GAAP net income for the quarter totaled $25 million overall, and this equated to $0.13 per diluted share. That compares to $12 million in non-GAAP net income in the year-ago period, which it was $0.06 per share. So more than double on both of those measures.

Year to date, our non-GAAP net income is $62 million. As we disclosed in the press release, we have generated $81 million of free cash flow during the nine-month period. So, we're quite pleased with the progress that we've made year over year, both in the amount of free cash flow, as well as the efficiency we are showing in driving and converting that income to free cash flow. This will continue to be a goal as we look ahead.

Now, let me close my remarks with some comments on our guidance. With one quarter left in the year, we are narrowing our annual guidance to reflect where we are year to date, and also incorporating some of the preliminary views I shared earlier on Q4.

Our full-year revenue guidance has been adjusted to $1.39 billion to $1.405 billion. This range anticipates the potential for variability in nonrecurring revenue in the fourth quarter. We're also narrowing our adjusted EBITDA range to a range of $238 million to $245 million for the year. And, finally, we are similarly narrowing our non-GAAP EPS range to a range of $0.45 to $0.47 per the year.

It's our intention, as is customary, to provide our view on 2016 during our fourth-quarter call in February. So, with that I would like to open up for questions. We're happy to start, operator, whenever you're ready.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Your first question comes from Richard Close from Canaccord Genuity.

Richard Close - *Canaccord Genuity - Analyst*

Just really quick on the bookings -- congratulations on all the success there -- I was wondering if you could -- I know you wait to fourth quarter for 2016, but how should we think about the potential for bookings growth over 2015?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

Richard, we've had obviously a really good run all year. Each quarter we've been up on a year-over-year basis. And we would certainly hope to keep that trend going in Q4.

Richard Close - *Canaccord Genuity - Analyst*

Okay. And then with respect to the pipeline, as you look out, you had talked about strength, both on acute and the ambulatory. If you can talk about the quality of the pipeline as you see it across your business units.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

We talked about strength not only in inpatient ambulatory but also post-acute. I'll let Paul maybe give more color but I think the results we saw in the quarter continue to show up in the pipeline as we look ahead, as well.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I think the things we've been talking about for 2015 continue in 2016, where we talk about growth in hosting and outsourcing opportunities, population health opportunities, the global marketplace, as well as new and replacement market. All those seem to be really coming into good focus. I wouldn't ever say we're hitting on all eight cylinders, but we're getting a lot closer. And that feels a lot better today than it did at any time we've been here with regard to the rate at which things are coming our way and, if you will, the clarity in the backlog.

Richard Close - *Canaccord Genuity - Analyst*

Okay. Congratulations.

Operator

And your next question comes from George Hill from Deutsche Bank.

George Hill - *Deutsche Bank - Analyst*

Good evening, guys. Thanks for taking the question. Rick, when you started talking about 2016, you had me excited, I thought we were going to get some guidance.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Sorry to let you down, George.

George Hill - *Deutsche Bank - Analyst*

It happens. Paul, can we talk about market segmentation? You guys are putting up good bookings. Can you talk about where you're winning, both on the hospital side and the ambulatory side, from a client perspective? What are the characteristics of a client right now who is choosing Allscripts competitively in the market? Why are you winning? And what prohibits you from moving up market? Baptist is nice and CHI expansion is nice. When do we see even bigger stuff start to roll in?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

The global piece, George, is also something to make sure we keep focused on with regard to moving up market, if you will. Those deals are pretty good size, the things that are out there that are, if you will, inflight.

In the US, I think the thing that you've covered, the large multi-group special practice organizations continue to look to us for both the EMR component but also the practice management component, and, importantly, for their capability to connect to the other organizations that they inter-operate in their communities. So, by definition, a large multi-group specialty practice is going to have to connect to the hospital in the geography as well as the ACO organizations and the insurance companies. So, that's been a good and will continue to be a great marketplace for us.

Those folks are also getting bigger, meaning they're buying other practices, and they continue to roll out all those solutions that I just mentioned. The hospital marketplace, everybody has one, or almost everybody has one today. And some of the people that are in that marketplace are moving out. They've either declared that a date certain point in time upon which they're no longer going to support the inpatient/outpatient revenue cycle system that people are currently on, and that's creating a marketplace for us to go after that wasn't here 12, 18 months ago. There are three or four suppliers that most people know about that have made that declaration.

There are other organizations who have made less investment on the, if you will, 2020 version of what a solution needs to look like that would include full post-acute, full population health, and full connectivity solutions. So, as people are looking from a hospital perspective at who is going to take them into the next decade, and what the next 10-year solution is going to look like, I think that's where we're getting more additional looks today than we may have in the past, to the extent that we can cover multiple different venues of care that they're moving into.

George Hill - *Deutsche Bank - Analyst*

Okay. That's all I had. Thanks, guys.

Operator

And your next question comes from Robert Jones from Goldman Sachs.

Nathan Rich - *Goldman Sachs - Analyst*

Hi, this is Nathan Rich on for Bob this afternoon. Just a question on the client services margin. It looks like you guys got back to the double-digit range, I think slightly ahead of your schedule. Can you just talk about what drove the upside there and how we should think about the margin opportunity for that side of the business going forward?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Yes. The variables that drive it, Nathan, we talked a lot about on our Q2 call. We had taken some pretty significant cost actions earlier this year, the latest of which was in May. When we finished our second-quarter call we said we didn't have a full quarter of that benefit in, and by having a full quarter benefit of some of those cost actions and aligning our resources and some of our service areas to the right level of demand, that that would naturally bring up third-quarter margins. So, some of what you are seeing was just basic math.

We also told everybody that we had renegotiated our hosting agreements last quarter. And that we expected those benefits to start to phase in at the very end of this year and more likely in first quarter. We started to pick up a little bit of that early. And that's partly why we got to where we got to as quick as we did. But low double-digit margin in services was something we forecasted three months ago, and I see it as just delivering on what we said.

Nathan Rich - *Goldman Sachs - Analyst*

That makes sense. And then just one follow-up. I just wanted to get your sense of how you're looking at M&A opportunities in the market right now. Obviously you made the investment in NantHealth earlier this year. Just would be curious, given some of the changes we've seen in the market, and any changes in valuations that you guys are seeing is, how you think about the opportunity to bolt on to your existing portfolio.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

Look, we've heard a lot of announcements. We all have heard a couple of announcements in the last quarter so there's a lot of activity out there. We're a pretty highly fragmented industry for what has become a more and more mature industry. I think some kind of evolution will likely happen and we think we've earned the right to participate in that.

We weren't executing so well a couple years ago but we think we've really gotten our act together, our class base together, our cash generating ability together. So, we will be active considerers of that. But we don't feel like we have to do anything but we'll certainly look for the right opportunity.

Nathan Rich - *Goldman Sachs - Analyst*

Great, thank you.

Operator

And your next question comes from Michael Cherny with Evercore ISI.

Michael Cherny - *Evercore ISI - Analyst*

Nice job on the bookings performance. Obviously we're now, I think, two-and-a-half years post the dbMotion acquisition integration. It seems like this is a business that, I know, Paul, when you first joined and acquired the business, you talked about it being incredibly strategic. As you look back now, has it lived up to your expectations or exceeded them? And relative to competitive dynamics on dbMotion who do you see as your biggest threat?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I always have very high expectations. I would say that almost invariably I'm going to get disappointed in that regard. I think from a pure play performance perspective of financials it probably has not been as solid on an independent basis as I would have liked them to be. I think, though, if you add it into the overall picture of what Allscripts represents today versus what we would have represented back in 2012 on the trajectory that we were on, it's very difficult to hold yourself out as a population health management supplier of tools and services to people if you don't have a layer that allows you to connect multiple different platforms, which is what this does.

It also does it -- to your competitiveness question -- in a way that nobody else that I'm seeing in the marketplace does it. This is third parties that are out implementing them as early as today continuing to review with me the fact that it's got a leg up. And that is that we not only connect different electronic medical records, and we semantically harmonize the data, putting it into a place where the data can be analyzed, but, importantly -- and this is the thing that really makes a difference, I think, between this solution and others that are out there -- you can as a physician get a delta view of the data that are important to you since the last time you looked at it, when you click on the community tab. And I don't have to, if you will, do a lot of signing in and signing out.

So, from a work flow, from an ease of use, from a value of data that are transferred to a very busy, highly, if you will -- they've got a lot going on each and every day, trying to see a lot of patients, this is the solution that really brings all the great and wonderful analytics that everybody is reading about, pontificating about, it brings it to the bedside of the clinic. At the end of the day you have to have and we have to offer solutions that allow that to occur.

Michael Cherny - *Evercore ISI - Analyst*

Thanks, Paul. That's helpful. One quick one for Rick. We're not trying to get rid of you yet but any update on the CFO transition?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

That would be me. I think it's a great honor for Rick that we have this high-class problem of looking for a CFO. I would just say publicly that he's been promoted as a result of myself and the Board's confidence in him and his capabilities as being able to take on more of the day-to-day operational responsibilities of the Company. We've retained a third-party search firm. We're going to do a national search. We will keep you updated on that process.

Michael Cherny - *Evercore ISI - Analyst*

Thanks, Paul, I appreciate it.

Operator

And your next question comes from Garen Sarafian with Citi Research.

Garen Sarafian - *Citigroup - Analyst*

Good afternoon, guys. Thanks for taking the questions. On sales, Rick, I think I understood your comments in the prepared remarks, but given some of your peers' results recently, I just wanted to touch on revenues again. In terms of sales, you discussed the puts and takes leading to your guidance. It all sounded pretty reasonable. But are you seeing any changes to industry trends impacting how your clients are spending, how much your clients are spending, or maybe other trends in how backlog is converting to revenue?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

I think the demand feels good to us. Again, three quarters in a row of record bookings. So not just comps off of what you might -- if a cynic said, hey, it's just up over poor comps -- these are actually records for the Company. So we're feeling pretty good about the demand profile, and pipeline feels good, too.

I think the conversion of bookings to revenue, especially when we think about some of the new services offerings that are coming to market, there's probably a little longer tail emerging. We're not just selling software that gets turned on one quarter out or two quarters out and therefore that triggers revenue recognition. There's a lot of services components that do require a little slower ramp. I think that's just maybe a general observation, but I don't see it as distorting our top line or anything like that, no.

Garen Sarafian - *Citigroup - Analyst*

Okay. That's useful. And then just one quick one, just to make sure -- Catholic Health is not included in the bookings number this quarter, is that correct?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

No, Catholic Health is in the third quarter bookings.

Garen Sarafian - *Citigroup - Analyst*

Is included. All right. Great.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

The one that's not is Paul spoke about a win with Advocate. And that's a very meaningful piece of business for us, and that will be in the fourth-quarter numbers.

Garen Sarafian - *Citigroup - Analyst*

Sounds good. Thank you.

Operator

And your next question comes from Greg Bolan with Avondale Partners.

Greg Bolan - *Avondale Partners - Analyst*

Thanks, guys, for taking the question. Just first, just a quick question, can you give me employee headcount as of the third quarter, please?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

It's not something we disclose typically. At year end we'll have something in our 10-K about employees. Let me just say, not to be mysterious, you won't find it having changed very much from last year end. We have gotten some efficiencies in some of the services and support areas, but we've seen some growth in some of our managed services, which require employees.

I'm not sure what analysis you're ultimately doing, but at the risk of stating the obvious, make sure if you're doing any kind of metric per employee that you're also cognizant of contractors, because there's an awful lot of hired labor that people don't report as employees, too. We've aggressively managed that down here, and that's a large part of our profitability story. I'm not so sure that's true around the industry, though.

Greg Bolan - *Avondale Partners - Analyst*

No. You certainly noticed where I was going. But is it fair to say, though, that just overall productivity per employee has improved? Because just annualizing this quarter's non-GAAP operating income and just taking that employee count from last year, obviously you take into account -- of course, also, you guys are hiring more on the outsourcing, outsourcing more staff -- but is it fair to say that that number has gone up per employee?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Profitability per employee?

Greg Bolan - *Avondale Partners - Analyst*

Profitability per employee, yes.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Absolutely.

Greg Bolan - *Avondale Partners - Analyst*

Okay, thank you.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Before you were cut off, the last thing, again, I'm not sure where you were ultimately going, but remember, too, that not all employees necessarily are -- you can't use the same cost estimate. We have, for instance, more than 25% of our workforce in low-cost labor markets.

Greg Bolan - *Avondale Partners - Analyst*

Thanks, guys.

Operator

And your next question comes from Matthew Gilmore with Robert Baird.

Matthew Gilmore - *Robert W. Baird & Co. - Analyst*

Good afternoon. Thanks for taking the question. I just wanted to ask about fourth-quarter EBITDA and margins. I think the implied range for the fourth quarter EBITDA has a nice step-up in margins from the third quarter. So, can you help frame up what's driving that sequential increase? Is that just the operating leverage and all the cost reductions that have gone on?

And then, secondly, you're obviously exiting the year at a much higher run rate for margins from the beginning. Is the margin range from the last two quarters a good jumping-off point as we think about next year?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Let me take those in order. Your observation on EBITDA, I'm not sure where you got that from. So let's just repeat. We just published a quarter where our EBITDA margin was 19%. I think if you look at the revenue range and EBITDA range that I put out there and the implied numbers for Q4, it depends where you are in the range and whatnot, but you're in the same zip code plus or minus 100 basis points. So I don't think there's any implied significant step up in EBITDA margin in Q4.

But maybe to the point, the second part of your question, is the margin performance durable going forward. Yes. I tried to make those comments to that, so let me just repeat them. Our gross profit margins are at the highest they've been, at least in the last three years here, and they came up a lot. The good news is we think most of that increase is durable. We did have a little bit of favorable mix in our software margins this quarter, and mix can change from quarter to quarter. So, you could potentially see a little bit of volatility or a little bit of degradation there depending on mix. But the pieces that go around that software mix we think are very durable, so I do think it's a good jumping off point.

Matthew Gilmore - *Robert W. Baird & Co. - Analyst*

Congrats on the quarter.

Operator

Your next question comes from Sean Dodge with Jefferies.

Sean Dodge - *Jefferies & Co. - Analyst*

Hi, good evening, thanks. Paul, maybe taking the market or booking segmentation question a little different way, you mentioned new clients continuing to be an important contributor. What percentage of bookings is coming from outside your current footprint? And which product specifically are you getting the most traction with attracting new clients? Is it mostly dbMotion or pop health or ambulatory or something else?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I don't think we gave the breakdown of what percentage comes from new business. But it was as good a new business quarter as we've had in a very long time. In this quarter, as we stated, I was very pleased with that from the standpoint of the range at which across the different business units that business came from. We had new business in dbMotion with the health plan, we had new business out of global which is important, we had new business in the United States in Sunrise. We have a bunch of new business in the TouchWorks organization and in the Pro organization. A lot of Homecare, which was extremely important to us because of the way that that connects the community and allows us to have a very strong and continued robust offering in the post-acute space.

So, quite frankly, as I said earlier, while we may not have hit perfectly on all eight cylinders, it's pretty close with regard to new business performance this past quarter. And it came from all of those different segments. Going forward, as you look at the pipeline, as we look at the pipeline, it continues to look good as these people that have been in the roles now for two-plus, in some cases we've got people that have been there for 18 years, but a lot of the team, a lot of the leadership has been here for a period of time, and you get productivity out of that leadership every quarter that they are spending more time in front of the same client. So, my indicators are feeling much better in that regard, and my expectations for the new business contribution continue to go up every quarter.

Sean Dodge - *Jefferies & Co. - Analyst*

Okay. And then you're a few months out now on the partnership with NantHealth. The long-term plan is to develop some pretty sophisticated solutions with them. But can you give us a sense of how long it will take to complete at least the initial integration of the two systems and maybe when we could first expect to see some form of co-branded solution hit the market?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I don't know that we're going to see a co-branded solution. I think the fact that there's a cross investment, go through the NantHealth medium as they go to market, or they'll come under our banner as we go to market inside of our installed base. But we should see some of their protocol algorithm machine work integrated inside of our organization, both TouchWorks and Sunrise, inside the next six months. So, we should see demonstrable benefit from that piece of the relationship very soon.

We're getting a fair amount of traction by having conversations with existing clients. And, as well, it's a pretty interesting dialogue with new clients as to what they think about, as I mentioned earlier, picking a 10-year electronic medical records supplier and partner for the next 10 years. Not only do they want the EMR, not only do they want connectivity platforms, not only do they want to be able to engage consumers, but they're also looking for a precision medicine platform. And we feel we're the only supplier out there that offers all four of those.

Sean Dodge - *Jefferies & Co. - Analyst*

Great, thanks. And congratulations again on the quarter.

Operator

And your next question comes from Charles Rhyee from Cowen Company.

Charles Rhyee - *Cowen and Company - Analyst*

Thanks guys. First of all, congrats on the quarter here. A quick question for Rick. Obviously we have now turned positive in revenue growth. Clearly your commentary in the past as we layer on the recurring revenues and bookings. Obviously you gave us the guidance for fourth quarter. Should we feel comfortable in how you had laid out, at least in broad strokes, the progression should continue, at least as long as our booking performance remains in this kind of range, that the revenue growth should start to continue to accelerate from here?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Charles, we've been fighting a trend all year, when we talk about revenue growth, we've been fighting a trend all year where recurring revenue has been growing at a pretty nice clip, and the nonrecurring has been going down a lot. I think we've talked about that at fair amount of length over the last three earnings calls.

The comment I made earlier in my prepared remarks was just to illustrate or let you know that I think the range that I can see for the near term on what nonrecurring should be is a range we've now been in the last few quarters. So, we should be done anniversarying these really large year-over-year declines, and then therefore that should allow the goodness, if you will, that's happening on the recurring side to show through. So, that's how I think about the revenue situation.

Charles Rhyee - *Cowen and Company - Analyst*

Okay. Then maybe to follow up on that, in that $80 million to $90 million, what does that mix consist of? We've now seen it being stable. What are people buying in that bucket?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

There's two significant buckets, is the way I should say it. One is what we classify up in our software, which is called system sales and others, and that picks up, Charles, to the extent we still do have upfront license software, and there's still some solutions that lend themselves to that, that's in there. To the extent we still have hardware attached to a deal, that's in there. And frequently we have third-party software that is part maybe of a larger sale or solution that integrates to our solution. Those are the types of things that tend to drive that system sales and other.

Then the second piece of nonrecurring is down in what we call other client services, and that's really that project-based work that I've talked about many times where we're usually either doing installs or upgrades of some of our solutions somewhere. So, collectively, that's the nonrecurring, and those are the two piece parts. If you pull out table 2 on the supplemental data sheet you can see how that's trended over time, each of those.

Charles Rhyee - *Cowen and Company - Analyst*

Right, okay. And last question just on the hosting margins, we've obviously hit the targeted low double digits. I can't remember off the top of my head, did you give us a sense of what you think it could eventually get to in hosting? What's the next target that you're looking for? Thanks.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Let me just make a clarification. When we talk about services margins, we're picking up more than just hosting. We're picking up everything that we put in that services bucket. Where hosting is I think worthy as a subset of all that, and it's worthy of a separate conversation, that has historically been a financial drain for us, and it's been an area of a lot of emphasis to improve our profitability there. As I said last quarter, we started that profitability improvement in March by restructuring a couple of our large third-party provider deals.

We've started to get some of that benefit already, and that's how we have achieved the jump up to double-digit profitability in services a quarter earlier than I had anticipated. But there's a little more there to get. So, we're going to continue to work. I think intrinsically services margins ought to be able to get those up to the 20% range over time. But that's not going to happen overnight.

Charles Rhyee - *Cowen and Company - Analyst*

Great. Thanks a lot, guys.

Operator

And your next question comes from David Larsen with Leerink Partners.

Chris Abbott - *Leerink Partners - Analyst*

Thanks and good evening. This is Chris Abbott in for Dave. And I also say congrats on the nice quarter and the strong bookings. The bookings mix this quarter, it was much more heavily weighted towards the client services, and I think historically it's been heavier on the software. What were the large buckets that drove that shift, even if we look compared to last quarter? Was it large contracts, or should we think of it being more heavily weighted going forward on the services side?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

I made a couple of comments earlier that would help to explain that a little bit. First off, Paul spoke at length and we also did a press release on our Catholic Health initiatives deal. That's a good-sized deal that's 100% services. So, that certainly helped. We had the two large Sunrise new footprints, both Baptist Pensacola as well as South Manchester. Those have a lot of software content in them, but they also have a lot of services content in those deals, as well. So they help drive both buckets, if you will.

Those would be a couple of noteworthy. But we, generally speaking, are underpenetrated across our client base in terms of providing services, certainly if you look relative to one of our larger competitors. And it's an area of good opportunity for us. So we'll keep doing that. Paul already signaled a nice win we've already booked here in the fourth quarter with Advocate Health. We're hoping to continue to have strength in that services line.

Chris Abbott - *Leerink Partners - Analyst*

Okay. And sorry if I missed it, did you restate the bookings, the software versus services bookings for the first two quarters? It looks like the table 1 chart in the financial supplement might have changed a little. Was there anything there that shifted?

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

This is Seth. There's nothing that shifted. We can look at that.

Chris Abbott - *Leerink Partners - Analyst*

Okay. Thanks, guys.

Operator

And your next question comes from Mohan Naidu with Oppenheimer.

Mohan Naidu - *Oppenheimer & Co. - Analyst*

Thanks for taking my questions. Paul, Rick, congrats on the good quarter here. I just want to hit on the client services bookings again one more time. You guys are getting higher mix of client services bookings than historical rate here. How should we think about the revenue conversion? Rick, you commented a little bit about that earlier, but should we start thinking about an elongated conversion from bookings to revenue?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

I wouldn't make any major shifts in your thinking at all. I was asked about are there any trends, and I think some of the services opportunities ramp up over a longer period of time. But there's a lot. Those are merging service areas of opportunity, and that's how I was answering the question. The basic managed IT programs, the basic services content around a new footprint, install, et cetera, and that's what's driving the lion's share of the numbers. Those are not having any different conversion right now.

Mohan Naidu - *Oppenheimer & Co. - Analyst*

Got it. That was helpful. Just one more question. Your earlier comment that you have a lot more opportunity within your own customer base for additional services, given that backdrop should we expect to continue to see higher mix of bookings coming from client services than software?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Look, we're a software company, and we want to sell a lot of software. We've had very strong mix the first two quarters of the year on the software side. Two-thirds of our revenue today is, as you can see from our P&L, what we would characterize as software and the delivery of it, and one-third of it is on services. When you look at it that way, us having one-third of services revenue, is a lot lower penetration than, again, one of our large competitors. So, it just to us speaks of opportunity, and it is opportunity we intend to exploit. But we still want to sell a lot of software.

Mohan Naidu - *Oppenheimer & Co. - Analyst*

All right. Thank you very much.

Operator

And your next question comes from Nicholas Jansen with Raymond James.

Nicholas Jansen - *Raymond James & Associates, Inc. - Analyst*

Hey, guys, lot's been covered so I'll just be quick. In terms of the UK opportunity, it seems like you've had several notable wins over the last couple of quarters. I just wanted to dig a little bit deeper there. The Oasis acquisition about 15 months ago. Just wanted to get your broader views of how you view the UK market shaping up and your competitive positioning in that market. Thanks.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I think there's a fair number of trusts that are over there that are making decisions about what they're going go do over the next 12 to 24 months. Our competitive position over there continues to increase, not only by getting new footprints but importantly the folks that are in country are highly referenceable for Allscripts. And that's the thing we've focused on very heavily. And that's the historical clinical side. Having a PAS solution that complements an EPR solution over there, in some cases, that was a reason why we might have not been invited to a procurement. And those reasons have now gone away.

There's also a fair amount of population health, community connectivity thoughts that are underway there, too, that helps our overall competitive positioning that perhaps two or three years ago they weren't including in their selection and evaluation criteria. The market is warming up. The solutions that we have are delivering results. And we have a number of executives over there who are willing to speak on our behalf about their experience with us and about the value that we've been able to jointly create. In this business, that's what you want clients to talk about. You want them selling for you. And as long as we can continue to give good support to those folks, which we plan to do, we expect to continue to win business over there.

Nicholas Jansen - *Raymond James & Associates, Inc. - Analyst*

Nice job on the quarter. Thanks.

Operator

And your next question comes from Gene Mannheimer with Topeka.

Gene Mannheimer - *Topeka Capital Markets - Analyst*

Good afternoon. I think that's Gene Mannheimer with Topeka. Congrats again on a good quarter. You've clearly done a solid job improving margins across the organization. When we think about going forward here, which of your OpEx line items do you think would have the best opportunity to leverage?

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

Which OpEx, Gene? Is that what you're saying?

Gene Mannheimer - *Topeka Capital Markets - Analyst*

Yes.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I will tell you how I think about it, Gene. I think of, there's three basic buckets of costs. There's our development investment, there's our SG&A cost, and then there is what we call our cost of sales, but the direct cost of providing some of the services. We've been hacking away at SG&A pretty hard for the last couple of years and feel good about the progress I've made there. It's an area we'll continue to emphasize, keeping a lid on it, so that we get really nice leverage off of that as we grow. But I don't think there's a lot more reduction to happen there.

In the same way, we're pretty committed to continuing to invest heavily in the solutions, so I don't see the R&D piece coming down a lot. But I do see opportunities in the cost of sale bucket. It's a collection of a lot of stuff. It's labor but it's also a lot of third-party providers that are somehow attached to some of our solutions. And we think we see some opportunities there.

So, that will be one of our areas, the focal point, in 2016. To the extent we're successful that should create some upside opportunity on gross profit margins. And then if you get that, that obviously gets leveraged all the way down the P&L.

Gene Mannheimer - *Topeka Capital Markets - Analyst*

Great, that's helpful, Rick. Thanks. And also I want to ask, with the ICD-10 deadline now behind us October 1, did you see in the quarter any impact of that on your client base and bookings, either good or bad? Thanks.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I wouldn't say that we saw it too much on the bookings side given the fact that our ICD-10 solutions have been out and available for more than a year. We put those in at the same time we put in the MU2 version of our software. So those were decisions, quite frankly, got made 12 to 18 months ago. There were a few laggards that realized one day that they needed to jump in, and we worked like crazy to get them ready and converted and get them over. That was work that's behind us.

I think, as has been the case around the rest of the industry, because of good planning, because of our clients' good planning in collaboration in working with us and just doing a lot of hard work on their end with the testing and working with their payers, there's been a remarkably small amount of, if you will, static around that coming out of the marketplace. I, quite frankly, expected there to be more and for us to be geared up to go quickly remedy anything. And we have not spent a lot of time on that.

We not only see it on the practice management side and the billing side, but we also see it with Payerpath where we are the back office EDI system for getting information submitted, the claims submitted to the insurance companies in multiple different payers. Again, very little issues there, which we're proud of. A lot of work went into that.

Gene Mannheimer - *Topeka Capital Markets - Analyst*

Thank you, Paul. Appreciate it.

Operator

And your final question comes from Eric Percher.

David Ho - *Barclays Capital - Analyst*

This is David Ho on for Eric. I wanted to switch gears a little bit and talk about the payer and life sciences business. I know in the past couple of quarters it's been a source of strength, but was just generally wondering if you could talk about how the unit has grown, what are some of the key drivers of that strength and maybe more specifically if you could talk about the partnership with Express Scripts and how that's doing. Thanks.

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

I would just say our payer life science business opportunity is meeting or exceeding the goals we had for it this year. It's obviously been a meaningful contributor to some of our sales throughout the first nine months of the year. And we're busy working hard to convert those sales into revenue, and I think that will become a more meaningful revenue contributor as I look ahead to next year.

I wouldn't want to comment on any specific relationships right now but we have a broad client base across payer and PBM communities right now. So, it's good.

Operator

And there are no further questions.

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

Okay. We have some closing comments, please.

Rick Poulton - *Allscripts Healthcare Solutions, Inc. - President & CFO*

I'm going to turn to Paul to close but I want to -- Chris some time ago had asked a question about whether we had a restatement on our bookings classification. And the answer is we did have a small just line item adjustment. Nothing changed in the totals at all. But, as with some of the new service offerings we are rolling out, we looked at it a little harder and split some of those between software and services as opposed to keeping them all in one category, so we thought it was appropriate to reflect them on a good comparative basis.

So, that was a good catch on your part. Sorry we didn't have the answer up for you initially. But there was a small change. If there's any more details anybody wants on that they can talk to Seth off line. Paul?

Paul Black - *Allscripts Healthcare Solutions, Inc. - CEO*

Thanks, everybody, for taking time to be on the call with us today. Clearly our Q3 is a reflection of a lot of hard work over a very long period of time. It's also been in collaboration with a lot of clients who have been continuing to vote with their wallet and with their fingertips as they give us better client ratings from many of the third-party rating agencies. So we're very pleased with where we find ourselves and this management team 36 months into the roles that we've had here. We've made a ton of progress.

We always can do better and we always will strive to do better, on behalf of our clients as well as on behalf of our shareholders. But I would just let everybody -- remind them that we are working very diligently on all the right things that we think move the meter, both on top line, bottom line, expanding margins, and growing this business in a profitable way. And, importantly, doing that with the right kind of relationships in the marketplace that earn us additional business with each one of our existing clients as we operate with them each and every day. Thank you very much for your time. We will look forward to talking with you all soon.

Operator

This does conclude today's call. You may now disconnect.
