THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

MDRX - Q4 2017 Allscripts Healthcare Solutions Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 15, 2018 / 9:30PM GMT

OVERVIEW:

Co. reported 4Q17 non-GAAP revenues of $547m, non-GAAP net income attributed to Co. of $33m and non-GAAP EPS of $0.18. Expects 2018 non-GAAP revenues to be $2.15-2.25b and non-GAAP diluted EPS to be $0.72-0.82.

CORPORATE PARTICIPANTS

Dennis M. Olis *Allscripts Healthcare Solutions, Inc. - CFO*

Paul Black

Richard J. Poulton *Allscripts Healthcare Solutions, Inc. - President*

CONFERENCE CALL PARTICIPANTS

Alexander Yearley Draper *SunTrust Robinson Humphrey, Inc., Research Division - MD*

Anne Elizabeth Samuel *JP Morgan Chase & Co, Research Division - Analyst*

Charles Rhyee *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Eric R. Percher *Nephron Research LLC - Research Analyst*

George Robert Hill *RBC Capital Markets, LLC, Research Division - Analyst*

James John Stockton *Wells Fargo Securities, LLC, Research Division - Director & Senior Equity Research Analyst*

Richard Collamer Close *Canaccord Genuity Limited, Research Division - MD & Senior Analyst*

Ross Jordan Muken *Evercore ISI, Research Division - Senior MD, Head of Healthcare Services and Technology & Fundamental Research Analyst*

Stephanie July Davis *Citigroup Inc, Research Division - VP & Senior Analyst*

PRESENTATION

Operator

Greetings, and welcome to the Allscripts Fourth Quarter and Full Year 2017 Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Mr. Dennis Olis. Thank you. Please go ahead.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Thank you, Darin, and thank you very much. Good afternoon, everyone. Our speakers today are Paul Black, Allscripts Chief Executive Officer; Rick Poulton, our President; and myself, Dennis Olis, Chief Financial Officer.

We'll be making a number of forward-looking statements during the presentation and the Q&A part of the call. These statements are based on current expectations and involve a number of risks and uncertainties that could cause our actual results to differ materially. We undertake no obligation to revise these forward-looking statements in light of new information or future events. Please refer to our earnings release and SEC filings for more detailed descriptions of the risk factors that may affect our results.

Also, as management reviews the fourth quarter details, please reference the GAAP and non-GAAP financial statements as well as the non-GAAP tables in our earnings release and the supplemental data book that are both available on our Investor Relations website.

And with that, I'm going to hand the call over to Rick Poulton.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Okay, thanks, Dennis. Good afternoon, everybody. We hope everybody's new year is off to a great start, and thanks for joining our 2017 year-end earnings call.

2017 was a transformational year for Allscripts, so I want to spend a few minutes discussing some of the moves we made and how that leaves us positioned going forward and then I'll then briefly talk about some of the client-specific accomplishments during Q4.

During the fourth quarter, we closed our acquisition of the McKesson EIS portfolio. We signed a letter of intent to acquire Practice Fusion, and we signed a letter of intent to sell the OneContent business, which, again, came to us as part of the McKesson EIS portfolio and we're selling that to Hyland Software.

And so then today, we announced the closing of the Practice Fusion acquisition as well as the signing of a definitive agreement for the OneContent sale.

So the net of all this activity is that -- the following: We've added hundreds of new client relationships to Allscripts for clinical, financial and data solutions; we have filled in solution gaps to our EHR portfolio in important market segments, where we're previously underrepresented; we have created what we believe to be the largest actionable outpatient clinical data set and the largest platform to efficiently bring payer and life science companies to the point of care; we have created significant cost scale and an opportunity to meaningfully increase EBITDA margins in the future; we've added significant talent to the organization; we've added a net of more than $300 million in recurring annual revenue to the company; and we've done all this for a very modest net investment of approximately $50 million.

So when we combine this activity with our previous corporate development initiatives as well as our organic efforts to reorganize and reposition certain assets for better growth opportunities as well as launch new solutions into new emerging growth areas, we feel very well positioned for the longer term. Dennis will share more color in a little bit about our outlook for 2018 financial performance, but we will achieve that largely through the hard work we've already done in positioning the company.

Where we stand today, roughly two-thirds of our revenue footprint is now represented by core clinical, financial, population health and managed services solutions to our inpatient and outpatient EHR client base here in the U.S. This is truly our core, and we will continue to focus on ease of use of our solutions, lowering the cost of delivery and earning a greater share of clients' wallets in the space.

It's no secret to any of you on this call that these clients in the U.S. continue to feel financial pressures from the changing regulatory and competitive landscape. So on the one hand, long-term fundamentals remain strong for us as technology solutions should continue to afford them more efficiencies and lower the cost. But on the other hand, all investments are scrubbed harder and harder for ROI requirements. And as Paul will talk about in a little bit, sales cycles are extending and increasingly difficult to predict.

So we expect steady demand for solutions from these clients, and we continue to expect to be a net share shift winner of new clients in this area as our industry continues to evolve, but overall, we've built our forecast assuming modest growth with this portion of the client base.

The other third of our revenue footprint is represented by higher growth opportunity areas, and we believe it's highly differentiated from most of our competitors. These areas include: First, our Netsmart and CarePort subsidiaries, who, as we told you last quarter, are making great strides with clients in sharing and delivering on the vision of seamlessly connecting the traditional health care provider networks and the post-acute health care provider networks. This is a challenge of ever-increasing importance and nobody has the scale or market presence that we do to make this a reality.

Second, our payer and life Science businesses. We see tremendous opportunity to continue to bring efficiencies and access to these two important players in health care delivery. The acquisition of Practice Fusion was essentially a doubling down for us in this area, and as I said earlier, we believe we now have, by far, the largest actionable clinical outpatient data set in the industry. We expect to continue to see strong growth in this area.

Third is our EHR-agnostic care tools including dbMotion, EPSi, FollowMyHealth and 2bPrecise. Each of these solutions have a growing list of clients outside of our EHR base, and they deliver industry-leading solutions in increasingly important challenge areas for healthcare providers and employers. These challenges include data aggregation and true harmonization of data, they include cost modeling and financial decision support; these challenges also include patient engagement and empowerment; and lastly, these challenges include care protocols based on genomic testing and results.

We continue to invest heavily across all these solutions as they tackle the challenges in these important areas, and we see these as significant growth areas for us in the future.

And finally, our growing international footprint and résumé of successful delivery sets us up well for continued strong growth outside the United States.

So with that overview of the markets we are addressing and how we see ourselves positioned for the future, let me shift gears and put a bow on 2017 with a few comments on fourth quarter client activity.

I'll start in the U.S. health systems market. As Paul will discuss in some more detail, we had the largest, most comprehensive Sunrise platform go live in years at Baptist Pensacola.

Also, we had a nice early return on our EIS acquisition as we put together a combination of Sunrise, inpatient and outpatient clinicals with some newly acquired EIS solutions to win a competitive process at Dearborn County Hospital.

And finally, Robert Wood Johnson-Barnabas Health, a long-time user of Allscripts Sunrise and TouchWorks solutions, expanded its use of dbMotion to connect their non-Allscripts EMR hospitals and physician practices. In total now, more than 1,300 MDs are now connected via dbMotion.

Moving to the independent ambulatory segment, Allscripts strategy continues to focus on leveraging our significant installed base to drive cross-selling and add-on services to our physician clients. We continue to see strong interest from our clients in outsourcing their billing and collection requirements by adopting our Revenue Cycle Management Services. Sales were strong during the quarter and as this continues to expand, we will increasingly have more of our revenue in this area indexed to patient volumes at our clients. But for now, these volumes only drive modest variability in our results.

We also were pleased to expand the scope of our relationship with Optum in 2 places during the quarter. One of their larger practices adopted our Payerpath clearinghouse solution. This is tightly integrated with our practice management system, which they are -- were previously contracted for, and we hope that success here will lead to other owned practices making the same decision.

We also had their MedExpress business unit install TouchWorks at three of their industrial medicine sites. This was not part of the scope of the original contract and early returns on client satisfaction are very strong. So we're very pleased with how our Optum relationship is going and the opportunities to continue to expand that.

Finally, I want to mention, while this incident happened in January, not the fourth quarter, I want to also mention an unfortunate event that primarily impacted our ambulatory franchise. Four weeks ago, two of our data centers that we use to host applications for certain clients were attacked by a powerful ransomware virus. This malware had never been seen before by law enforcement and was the work of very sophisticated criminals. We took immediate measures to prevent the spread of the attack and protect all client data. To this day, there's been no evidence that any client data was removed, and we are grateful to our security and response teams for their efforts as we know others in the industry have not been so lucky during similar attacks.

We take data privacy and security very seriously, and we spend tremendous amounts of money protecting our data centers and our networks, much more than most every self-hosted client could ever afford to spend.

The lessons learned from this incident will help us get even better in the future in preventing and responding to such incidents, and we have been very busy communicating to our clients specific steps that we are taking to continue to improve.

So we hope that, that's behind us and look forward to continuing to rebuild and strengthen the relationships with our clients that were impacted by this.

Now I want to move to our international business. Like our third quarter, the fourth quarter was very active for our international franchise. We had another go-live in the U.K. with Maidstone and we continue to expand our footprint in Australia as we continue to expand the reach of the clinical systems beyond South Australia with several sales of the Sunrise-BOSSnet EHR platform to hospitals in Western Australia. These organizations are undergoing a transition from paper to electronic medical records and the Sunrise-BOSSnet platform is used to transition to digital order entry and ease the move from paper-based records. We see BOSSnet as an outstanding on-ramp to EHRs, where they do not exist today, and we're evaluating additional geographic opportunities to bring this to.

And finally, we went live in Costa Rica with Sunrise reg and sched functionality. This was delivered through an Azure public cloud instance. This is an exciting first for the company and we look to build on this momentum going forward.

Lastly, in our post-acute segment, Netsmart had a strong sales quarter, which continued recent trends. Netsmart added another 75 facilities during the quarter, bringing the total for the full year to approximately 600 facilities. These new clients represented almost 50% of Netsmart bookings for the year so they have a great balance in growing existing accounts while also adding significant new footprint.

So with that summary, let me turn the call back over to Dennis to go through the financial highlights for the quarter.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Great. Thanks, Rick. As we review this quarter's numbers, please reference the schedules in the earnings release as well as the supplemented data workbook available on the Allscripts website.

As a reminder, we closed the Enterprise Information Solutions transaction on October 2 of 2017 and began consolidating the results as of that date. As such, Q4 includes a quarter -- a full quarter contribution from EIS.

In Q4 and for the foreseeable future, we will provide the revenue contribution for EIS. However, since we have fully integrated the EIS business into the Allscripts call centers, we will not provide financial information for the former EIS business below the revenue line.

As previously reported, the financial results for Horizon Clinical and SERIES 2000 product lines are reported as discontinued operations in Q4 and through the product's end of life on March 31 of this year. My comments on the income statement will largely focus on non-GAAP metrics, unless otherwise stated. Full reconciliations of GAAP and non-GAAP figures are available in the earnings release.

All reference to Allscripts current results are made before considering the impact of industry-wide revenue changes in revenue recognition issued jointly by FASB and IASB as Topic 606 and IFRS 15, respectively.

With Rick having briefly discussed bookings and Paul following with more color shortly, I'll begin with backlog, which stood at $4.6 billion in December. This reflects both the impact of bookings as well as renewals in the quarter that are not included in the bookings metric.

The fourth quarter amount includes the addition of backlog from the McKesson Enterprise Information Solutions transaction. The software component of backlog comprises 59% of the total while service accounts for the remaining 41%.

Turning to the income statement. Fourth quarter non-GAAP revenue totaled $547 million, an increase of $117 million or 27% versus Q4 of 2016. Non-GAAP revenue adds $30 million in acquisition-related deferred revenue adjustments in the fourth quarter of 2017. In 2016, this adjustment totaled $4 million, and therefore, the Q4 2017 GAAP revenue growth is 22% versus the fourth quarter a year ago.

Netsmart's Q4 non-GAAP revenue totaled $85 million, growing 14% year-over-year.

EIS contributed non-GAAP revenue totaling $104 million. This includes the EIS portion of the acquisition-related deferred revenue adjustment of $27 million.

In Q4, we also recognized a one-time favorable revenue adjustment of nearly 10% of the reported EIS revenue associated with the acceleration of revenue from project-related work.

As we move into 2018, our non-GAAP revenue guidance for Allscripts reflects the removal of the one-time revenue adjustments in EIS that we experienced in Q4, the anticipation of future attrition in EIS as discussed on previous calls, and the removal of revenue and cost associated with the OneContent divestiture.

Looking at our total revenue split, total recurring revenue grew 32% and nonrecurring revenue grew 11% versus the same period a year ago. Thus, our total recurring revenue mix came in at 79% in Q4, 78% for the full year.

As we incorporate 606 revenue recognition changes into our 2018 reporting, we would expect to see more volatility in our recurring and nonrecurring mix.

Looking at revenue results by line item. Total software revenue in Q4 increased 25% year-over-year, totaling $354 million. Recurring software revenue consisting of subscriptions, recurring transactions, support and new maintenance increased 35% year-over-year. A large portion of this growth was driven by the consolidation of the EIS business.

In the quarter, nonrecurring software revenue decreased 23% year-over-year.

Given the multiple variables in these metrics, we anticipate quarterly fluctuations in nonrecurring software from quarter-to-quarter and would not view the Q4 percentage as reflective of our future results.

Turning to client services. Consolidated non-GAAP revenue grew 32% year-over-year to $193 million in Q4. Recurring service revenue increased 25% year-over-year, driven by the addition of EIS, revenue cycle services and other multi-year service offerings. Similar offerings from Netsmart such as hosting, revenue cycle services and managed services also contributed to this increase. Allscripts nonrecurring service revenue increased 47% year-over-year, driven primarily by additional revenue from implementations and upgrades.

Moving to non-GAAP gross margin. Total gross margin was down slightly, 30 basis points year-over-year. We anticipate gross margins to improve as we enter 2018 and recognize the synergies from the EIS acquisition. Analyzing revenue by component, software gross margin decreased by 50 basis points year-over-year. Client services, on the other hand, for Q4 came in at 16.7% compared to 14.8% for the same period last year. While gross margins on services are trending consistently in the mid-teens as anticipated, the increase also reflects the addition of EIS, which runs at a slightly higher service margin than core Allscripts.

Looking at operating expenses, non-GAAP SG&A totaled $114 million, a 15% increase year-over-year. The non-GAAP SG&A figure excludes non-cash transaction-related and other expenses. The increase in SG&A is primarily a function of the additional acquired expenses from EIS.

Gross R&D was $105 million, up 50% year-over-year, reflecting additional R&D expenses attributed to the acquisitions at Netsmart and Allscripts. Allscripts software capitalization rate was 30%, a step down from Q3. We anticipate a software capitalization rate in the low-30% range for 2018.

Adjusted EBITDA totaled $107 million, a 28% year-over-year increase. This equates to a 20% adjusted EBITDA margin. Netsmart's adjusted EBITDA was strong in the quarter and is trending in the mid-20% range as a percent of Allscripts total reported EBITDA, in line with our expectations and within the 2017 guidance range of between $90 million and $100 million.

Looking below the line, total cash interest increased 28% to $20 million, which compares to $16 million from a year ago. The largest contributor to this increase is the financing required to fund the EIS acquisition.

Please note that GAAP results this quarter included transaction-related costs, severance fees and other costs of $25 million, primarily related to the EIS transaction.

Finally, excluding non-cash adjustments and transaction-related and other expenses, non-GAAP net income attributed to Allscripts totaled $33 million and non-GAAP EPS was $0.18 for the quarter.

As a reminder, non-GAAP EPS is calculated net of noncontrolling interest to reflect Allscripts ownership portion of the partially owned controlled and consolidated businesses.

Non-GAAP net income attributed to Allscripts healthcare solutions, grew approximately 25% year-over-year.

Today, we also announced that we amended the Allscripts credit agreement providing for increase in available liquidity and tenure as lower interest rates. The amendment provides a $400 million term loan and a $900 million revolver facility. This represents an increase in borrowing capacity of $500 million. The maturity date was extended to 2023, approximately three years after our convertible notes mature.

Allscripts ended the quarter with a principal balance of $629 million in secured debt and $345 million on convertible senior notes, a [$59 million] increase in long-term debt quarter-over-quarter. This increase reflects the financing required to fund the acquisition of the EIS business.

Netsmart's total debt, which is nonrecourse to Allscripts but reported for consolidation purposes, totaled $646 million, down slightly quarter-over-quarter due to required repayments.

Turning to cash. Q4 operating cash flow improved by $22 million year-over-year to $106 million due to strengthening business results and contributions from the EIS business. Q4 free cash flow totaled $68 million after adjusting for capital expenditures, capital software and purchase software.

On a full-year basis, operating cash flow improved to $279 million, a 4% increase year-over-year. Free cash flow was $94 million versus $134 million in 2016. 2017 free cash flow was impacted by increased investments in development software. As we've noted in the past, cash flow will vary from quarter-to-quarter.

Turning to our outlook. We're initiating our 2018 financial outlook as follows: The company anticipates non-GAAP revenue of between $2.15 billion to $2.25 billion. We anticipate adjusted EBITDA to be between $420 million and $460 million. Excluding Netsmart, the adjusted EBITDA is expected to be between $310 million and $340 million.

Finally, we anticipate Allscripts non-GAAP earnings per share of between $0.72 and $0.82 per diluted share.

We have built our most recent acquisition of Practice Fusion into this guidance. In 2018, we expect this transaction to be marginally accretive.

Additionally, today, we announced our divestiture of the OneContent business, a portion of the business we recently acquired from McKesson. The impact of this is also reflected in our full-year guidance.

As stated in our Q3 call, we are reporting additional revenue and expense details attributed to the Horizon Clinical and SERIES 2000 businesses in our 10-K. These discontinued operations will wind down by the end of Q1 in 2018. And therefore, our outlook for the year excludes the impact of this discontinued operation.

As we move into 2018, we have adjusted our guidance for our expected effective tax rate of 27% for the full year 2018.

And with that, I'll turn it over to Paul Black.

Paul Black

Thanks, Dennis, and I'd like to acknowledge and congratulate Dennis on the interim role being removed from his title of CFO.

And I'll reflect back on 2017. In the past five years, I'm very proud of what this team has been able to accomplish. Thinking back, we've made a number of important decisions that have made 2017 the year that it was. We've invested in our core solutions, effectively spending the R&D to meet regulatory demand, increased solution breadth and depth and to innovate on the platforms we offer clients on a worldwide basis.

This has contributed to the multiple consecutive quarterly bookings records and on annual basis, we've been able to demonstrate client retention, attraction of new clients and cross-sell new capabilities to our existing clients, expanding our market share.

We've also invested in new platforms in anticipation of the world in a post stimulus market reality, creating a number of growth platforms outside of our core EMR offerings.

As we have been a team that has made and kept commitments with our clients and stakeholders, we have provided multi-year guidance and provided the models, which show the path in those projections.

Regarding bookings. I'd like to make the following observations. One, our bookings are for new relationships or expanded footprints to the company. We did not count existing client renewals in this number. We also do not count the value beyond 12-month maintenance stream for new deals.

Two, bookings in the United States are harder to predict as we are working on hundreds of client opportunities every quarter. The deals are getting bigger and at times, the timing of their closure does not align with the 90-day cycle.

Three, we have an exciting pipeline on a global basis. We have a new client base in EIS and as of yesterday, in Practice Fusion. The EIS base has been reactivated and will benefit from the additional solutions and services that Allscripts has to offer.

Four, our demonstrations to new clients in 2017 was an increase over 2016. We have also built a solid pipeline in the payer and life sciences, global, consumer and managed services businesses.

And fifth, included in our 2018 guidance, our revenue growth expectations beyond 2018 are the expectations for bookings. Of interest, given that we have roughly 80% of our revenues coming in on a recurring basis, the reliance on -- in year new bookings has decreased over time as a percentage of recurring has increased steadily over the past five years.

For the guidance we offer today, this represents about $300 million per quarter.

Turning to 2017 highlights. We had significant new client signings during the year and announced our largest Sunrise agreement ever. We went live in many organizations, highlighted with Baptist Pensacola, where a single platform was deployed for inpatient EMR, outpatient EMR, inpatient revenue cycle and outpatient revenue cycle; a Capstone event delivering on our investments and on the vision for an open community-based EMR all-in-one platform.

We also activated Sunrise at the Royal Adelaide Hospital in Australia, a brand new state-of-the-art 800-bed facility and the largest implementation in Australia.

We continue to be recognized by one of the industry's leading independent benchmarking companies, who utilizes the most comprehensive survey technology. Allscripts has remained #1 for EMRs of over 250 beds and for population health management for the past four years. This past Monday, we were selected as the #1 vendor for many of the global regions that we compete in also.

From a culture standpoint, I'm extremely proud of Allscripts give back efforts in 2017. We suffered three major hurricanes in the United States. In Texas and Florida, we've partnered with Surescripts to provide free access to patient-specific medication history to pharmacists. In Puerto Rico, we partnered with MedShare to deliver critical medical supplies to those in need. Allscripts employees dedicated thousands of hours of their time and thousands of dollars out of their pockets to help those impacted by these natural disasters. All of this is culminated in an exceptionally strong set of financials as highlighted earlier by Dennis. We enter 2018 with annual sales projected over $2 billion and climbing. We have created the scale needed to be a relevant, long-term player in this large and growing market. We are much stronger, vibrant company today that we were in late

2012, and we expect much more in 2018. We will continue to innovate, to create an open platform, which instills an entrepreneurial culture, which embraces third-party developers. We will continue to evaluate M&A opportunities, where it makes sense and where clients will benefit. There will be continued consolidation in both the EHR as well as in the post-acute market, and we will be active in those segments when it makes sense.

We will not be complacent with our success in 2017. We will continue to serve our clients in a manner, which will retain their trust and deepen their relationship with Allscripts. We are committed to providing the highest quality and service levels to our clients, which in turn, will benefit the patients that they care for.

With that, I'll turn it back to the operator to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Jamie Stockton of Wells Fargo.

James John Stockton - *Wells Fargo Securities, LLC, Research Division - Director & Senior Equity Research Analyst*

I guess, maybe the first one, just bookings, I don't know -- I'm sure, it's going to be a decent focus, and Paul, I understand you tried to address it somewhat. But it looked like the weakness was at least year-over-year in the services bucket. I think, Rick, maybe you, you said that RCM actually -- it seemed like it had a decent quarter, just any incremental color you could give there would be great.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. So I'll go first and then Paul. So RCM, yes, did have a good quarter, Jamie. It's one of many services offerings that we have. I think we saw less activity around outsourcing and larger managed hosting or other managed kind of more comprehensive managed services contracts that you might see in larger institutions. So remember, our rev cycle is, at this point, something we bring to our ambulatory clients. We have not delved into inpatient revenue cycle as of yet. But so those two, your observation is not inconsistent with what I was saying.

James John Stockton - *Wells Fargo Securities, LLC, Research Division - Director & Senior Equity Research Analyst*

Okay, that's great. And then maybe just one more on the OneContent platform that you guys are selling to Hyland. Just any numbers around that would be great, proceeds expected from the deal, how much revenue is getting carved out, EBITDA, that would be great.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, so revenue and EBITDA, Jamie, we've never done that at a product level or at a product-line level, so we're not going to start with this. I guess, I'd reiterate what Dennis said is our guidance -- I'd reiterate two things. One, our guidance reflects the transaction so we counted that in. And I'd also point you maybe to my comments where I said the net impact of all of our corp dev activities recently adds -- well, it's approximately $300 million in recurring revenue, not total revenue. So I think you could triangulate around that and make some decent guesses. Proceeds on the transaction, with respect to -- again, I'd give a number that the net of all that is about $50 million of capital. That's inclusive of transaction costs and things like that. So you'll see a lot of details when we file an 8-K on the transaction, but you should think of it as mid-200s of proceeds.

James John Stockton - *Wells Fargo Securities, LLC, Research Division - Director & Senior Equity Research Analyst*

Just Rick, the $50 million, does that also include the Practice Fusion transaction?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes, all three deals.

Operator

Our next question comes from Ross Muken of Evercore ISI.

Ross Jordan Muken - *Evercore ISI, Research Division - Senior MD, Head of Healthcare Services and Technology & Fundamental Research Analyst*

So maybe -- yes, you talked a bit earlier on international and some of the momentum there and obviously, you've had some good results in Australia. Can you just give us a feel for kind of the size or the scope of bookings that are available in many other parts of the world, in Asia or in the U.K., et cetera, just so we can get a sense for the upcoming year what that opportunity set looks like?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Sure. And I would also add to the prior question that international did not have a great Q4. When you -- if you look at places that were a bit off, it compares to what they've done over the rest of the year. So in the markets that we compete in, we are typically either selling Sunrise or we're selling dbMotion. So on average, those deals probably are 50% bigger than the average deal size here in the United States when they close, so something south of $20 million, but north of $10 million. And so they're pretty good sized transactions. The pipeline looks pretty decent, but as we have experienced over time in the businesses outside the United States, those are government-driven and government-led and has a rigorous procurement process that is less predictable on a quarter-by-quarter basis. We've got some pretty good-sized deals that we're working on, that are larger than that, but again, those are not something that we have talked about or projecting right now in bookings number that we would be using internally.

Ross Jordan Muken - *Evercore ISI, Research Division - Senior MD, Head of Healthcare Services and Technology & Fundamental Research Analyst*

Got it. And just on Netsmart. It seems like that business, the momentum, as you sort of say, it's been quite good. I guess, how are you -- you've added a few assets there, the internal is good, the margins are great. I guess, how are you just thinking about where that asset's situated right now? And what else you can do to kind of help unlock value there?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, our focus right now, Ross, is on growing value there. And I think we've accomplished a lot in what's not quite two years yet since we put that together. And that's the focus for now. So we continue to work with the management team and our other owner partner in the deal on strategies for growth and strategies for becoming a -- the de facto solution in some of the verticals that they participate in. The question on how do you unlock that value, I think we're going to continue to provide -- as we provided in the guidance, transparency on what's some of their contribution is coming from the asset, so that folks like yourself and folks like our investors can properly assess what the value of it is and therefore, what ownership stake is. And after that, we'll continue to think about it and when we make decisions, we'll let you guys know. But right now, the focus is on growing.

Operator

Our next question comes from Richard Close of Canaccord Genuity.

Richard Collamer Close - *Canaccord Genuity Limited, Research Division - MD & Senior Analyst*

First part of the question would be, is there any update in terms of the long-term targets that you have now that we're, I think, two years or so into that?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes. As far as the guidance that we provided, we've given the '18 guidance with all the moving parts. We haven't updated a three-year guidance at this point. Something we may consider later in the year. But at this point, we're just writing the 2018 guidance.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes, I think -- so I'll add to that, Richard, is, if you remember, we introduced the three-year kind of outlook at our Investor Day last March, which was meant to give you some -- give everybody a lens into how we thought about life beyond 2017. We updated that when we did the McKesson deal. And so then we kind of debated what do we do now, do we refresh one year, do we stick with this three-year? And we just thought it was more traditional and probably a little user-friendly -- more user-friendly right now to go back to the annual guidance, and that's what we've decided for '18. I think we'll -- as Dennis said, we'll think about it later this year and maybe either in our next investor session or before that, we'll come out with something about what our aspirations are behind those.

Richard Collamer Close - *Canaccord Genuity Limited, Research Division - MD & Senior Analyst*

Okay. And can you just give us a little bit of an update on the Practice Fusion? What are your thoughts in and around that acquisition now that it's complete? And just on a go-forward basis, where do you see opportunities, what do you need to do to make that a really good transaction for you?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, the product itself fits a void that we have. So it is the value solution. And we've talked for some time now about how we think about the EHR market in segments. We think about value solution, both in the inpatient and the outpatient world, and we think about more of a premium solution in both the inpatient and the outpatient world. And they're different solutions designed to meet different needs and clients kind of self select whether they want a more rudimentary tool or they want a more sophisticated tool. So that represents the value solution in the industry and I think is a great add to what we have already for ambulatory solutions. Why we did it though? As I said in my comments, Richard, it's -- their business model has been to use the clinical data they capture and the clinical presence they have at the point of care to bring the payer and life sciences communities to the marketplace. And we do that ourselves already, and so the combination with Practice Fusion, as I mentioned, kind of a doubling down for us in that opportunity set. And we really like the asset base we've put together, and we're looking forward to some good things happening in that space.

Operator

Our next question comes from Anne Samuel of JPMorgan.

Anne Elizabeth Samuel - *JP Morgan Chase & Co, Research Division - Analyst*

On margins, you've done a nice job of moving expenses out of the base for the past couple of years. How should we be thinking about your cost structure and ability to leverage expenses going forward here as you integrate some of these acquisitions? And is there any more room to cut?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes. Thanks, Anne. So from a margin perspective, we still have room to improve. When we talked about the EIS synergies that we expect to get throughout the course of the year, we talked about a pretty significant improvement expected as we work through 2018 going from the mid-EBITDA range for the businesses that we acquired to somewhere in the 18% to 20% range as we go into 2019, so you'll continue to see expansion in margins associated with the synergies that were recognized at EIS and to a much, much smaller extent, with Practice Fusion. We also, in the second quarter, mentioned that we had entered into an agreement with Atos, who is our hosting partner, and that's a long-term agreement that we have with them to consolidate some of our hosting facilities and generate additional savings in that regard. And then the third thing I would mention would be that we did -- we have noted that we are moving to -- in the ambulatory space a cloud-based offering. We'll talk a bit more about that at HIMSS. But again, that has an opportunity to improve our margins over the next few years.

Operator

Our next question comes from Eric Percher of Nephron Research.

Eric R. Percher - *Nephron Research LLC - Research Analyst*

Let's talk EBITDA guidance. If I look at the range and I take out Netsmart, we've got a $30 million variance from bottom to top, which I know is, what, two, three times what it's been in the past. You've got a lot more complexity this year, but how much of that range is revenue-dependent versus expense and margin-dependent?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. So first, the revenue, the range that we provided this year is slightly bigger, but again, I think that coincides with the fact that we've significantly improved -- increased our revenue over time. As it relates to the EBITDA, the variance and the range that we have, it's roughly at a 20% EBITDA margin at both the low end and the high end of that range, so it's really not cost-driven. We will continue to drive the cost initiatives that I just spoke about in the last question. But it's really revenue-driven in how we can recognize some of the growth opportunities that Rick and Paul have laid out.

Eric R. Percher - *Nephron Research LLC - Research Analyst*

Okay. And one notable item on the expense side would be the McKesson TSA. Do you expect -- I know you'd spoken earlier about your hope to move off of that earlier. Do you expect that, that's still mid-year or could it come earlier in the year? And is that meaningful?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

It is meaningful, and it's part of the guidance that we've provide that as we've talked about the improvements that we're going to see through the synergies that we're going to recognize over time. So as it relates to the TSA, there's many different components within that TSA. So we're still tracking to terminating the entire TSA by the summer, but we're able to move off certain components of that TSA sooner than we had originally planned, things like IT and some of the systems that we're working on, we anticipate moving off those a few months sooner than originally planned. So that's going well. We will continue to be off of TSA by middle of summer.

Operator

Our next question comes from George Hill of RBC.

George Robert Hill - *RBC Capital Markets, LLC, Research Division - Analyst*

I guess, for Paul and Rick. Paul, I want to check an assumption. It was interesting you kind of called out the Barnabas-Robert Wood Johnson deal where you guys sold dbMotion. I guess, first, should we think of that as basically eliminating any churn risk in that client? And then my follow-up question would be, how do you think about the experience of selling dbMotion into that client? And like how is that a leverageable opportunity as you think about the EIS customer base in a way to kind of minimize churn there?

Paul Black

Rick is the one that actually talked about it, but I'm happy to do it since I've been there recently, George. I would absolutely expect that a client like that, who has two extraordinarily capable electronic medical record suppliers, both us and the other folks that are in there. We have long advocated the positions of not reaping and replacing end user capital to use for other solutions like population health, like analytics and some of the other things that we supply. So we're very pleased as a result of their usage of dbMotion inside of the former Barnabas solution to bring that over -- or excuse me, the Robert Wood Johnson solution or sites to bring that over across the entire enterprise. So I would expect that to be a hedge against churn, to answer your question. And working with those guys, we worked with them for quite a while at HIMSS a couple of years ago. Bob was on the podium with us and he was talking about what they're doing with population health when he was just part of the Robert Wood Johnson organization and has been a long-term client there and has been a big believer and been a long-term supporter of what dbMotion could be. Broadly then, taking that dbMotion platform into other organizations, whether it'd be an all-Epic site or an all-Cerner site, it has a lot to do with who they're attached to in the marketplace, not only are they affiliated in the own physician practices, if you're a large -- speaking about large IDN, but also in the post-acute arena, where they are increasingly more interested in having that data come in to a single harmonized data set that they can actually perform the analytics on. When you're accountable for those people financially, you want to know what they're -- where they've been and how much they've consumed inside and outside of the organization. With the -- specifically, with the EIS base, there's a lot of very large integrated delivery networks that has the McKesson STAR patient financials and the McKesson Medi-Pak or HealthQuest patient financials and that is another door that we can go into, if you will, through the CFO to have similar conversations about what their interoperability strategies are inside those organizations. Rick mentioned that there's a lot of ROI discussion and there's a lot of discussion around making sure that these people are spending the capital dollars that they have very wisely and dbMotion is popping up as an extraordinarily relevant topic these days.

George Robert Hill - *RBC Capital Markets, LLC, Research Division - Analyst*

Maybe if I can do a quick follow up. And I'll reach a little bit on this one. Any chance to sell that functionality into the VA?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

We certainly hope so. We have been talking to anybody that will listen to us in that ZIP code about what our capabilities are. We've been pretty active in that regard. There's no promises there, George. And until the total contract is actually let for who the EMR supplier is, then we will work with that person because that person will probably also be the prime contractor and that would be the person with whom we would deploy this type of technology if that's the way that VA decides to go. There's a reality to the environment there that we point out, and that is, over a 10-year period, you're going to have a DoD environment on a new platform, you're going to have a DoD environment on an old platform, you're going to have a VA environment on our new platform and you're going to have a VA environment on the old platform as you move from the east -- or from the West Coast to the East Coast. And also inside the VA, you've got 30% of the current record that's supplied through non-VA entities like community physician groups. So a very heterogeneous environment, all of which would, we think, play nicely to a very robust interoperability strategy that we are quite confident that we could produce at scale benefits for the VA.

Operator

Our next question comes from Sandy Draper of SunTrust.

Alexander Yearley Draper - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

I guess, first, and I apologize, I got on a little late, so Rick, you may have covered, but I don't think you did. I'm just trying to understand the -- you said there's $300 million of recurring revenue that is built into the guidance, I think that's correct. And I'm just trying to understand, did you break out sort of what total acquisition revenue is expected to be in 2018, thinking about Practice Fusion and any other? Or is it just right now, you're only focused on giving a comment about the $300 million of recurring revenue?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. Sandy, I -- my focus was on trying to synthesize all the corporate development activities that we've been involved in, in the last couple of quarters and let you try to cut through it all and see what the net impact of all that is. So that was my comments on $300 million of recurring revenue, that's been added at what was a very small capital cost to us. The issue as to what's in the guidance picture is, again, that's a little -- remember, a little apples and oranges. I mean, McKesson was in the numbers for all of Q4, so I'm not -- that you shouldn't think of that as an incremental statement. We also, obviously, are disposing of a business that was in the Q4 numbers as well. So I think the best way for you to think about it, Sandy, if you're trying -- I'm kind of reading between the lines, I think you're probably trying to think about organic growth versus nonorganic perhaps?

Alexander Yearley Draper - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

Yes, exactly.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

I think what you should do is start with what the Q4 runway was, listen to what Dennis told you about some unusual items that didn't belong in there, hair cut it for the business that we're getting rid of and then you could kind of multiply that times four and sort of start with, that anything growth beyond that is organic.

Alexander Yearley Draper - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

Okay, that's helpful. I appreciate that. And then the second question, just thinking about your comments about the continue -- or maybe it's Paul's, about continued consolidation in the industry. Your expansion of your debt capabilities. Just in terms of your appetite -- or I don't mean appetite -- ability to continue to do acquisitions. You've got EIS only at quarter in, Practice Fusion just closed. Does there need to be a pause button? Or do you feel like you've got the capability if another asset came to market, that you'd be willing to do it? Or do you really need to pause for a bit before you continue to look at opportunities?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes, I appreciate the question. We are not at all acquisition nuts all of a sudden. That is not our growth strategy. We think we accomplished a lot, both strategically and financially with the deals we did. And so -- and we're integrating those very well. Frankly, the integration on those is not that tough. So there's work to be done, but it's from a product rationalization side, it's not that soft. There's not much overlap, so the work is really more about getting the organization at the right cost structure, which is easier to control. So work to be done, but on the grand scheme of acquisition integration, not that hard. So then to your question, do we need to hit the pause button? I don't know about need. I mean, I'm certainly not looking to do anything today, but it's need isn't probably the way I would think about it. We're not going to race off and buy everything that's on the street. And believe me, there's lots of stuff available on the street, but we're going to be smart, we're going to be disciplined. We're big believers, and we've said it for years that the industry needs to evolve. It's going to happen, so we might as well happen and do things -- lead that charge and do things that make sense for us. So it's with that same filter that we'll look at other opportunities. Credit facility, that's just good old-fashioned business sense finance. We restructured our -- the tenor of our debt, we expanded it so we have more dry powder if we want it, but I wouldn't read too much into that.

Operator

Our next question comes from Charles Rhyee of Cowen and Company.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

So I appreciate the earlier comments around bookings that you did not include any kind of business with existing clients, it's all new client relationships. But when I look at the backlog, the ending backlog, up about 15% at $4.6 billion, if I were to kind of simply add new bookings in the quarter, subtract $546 million of revenues recognized in the quarter and then compare that to the end of quarter backlog -- last quarter -- in the third quarter, I see a delta around $770 million. I mean, is that may be indicative of business line with existing clients? Or am I kind of doing the math wrong there?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes, Charles. The way we determine backlog is different in the way we report bookings. So for example, when we have a large renewal for a client we have on a pretty regular basis, we do not consider that a booking in the quarter, but that -- but the value of that does fall into backlog. Because it's not a simple thing...

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Right. But so compared to, like, maybe some of your peers who do include renewals in the bookings number, if we were to think of it more like -- we could think of -- you do get critical about it, right, because that ends up going into revenues in the future?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes, you're correct, and that's why we include that in the backlog number, but we do not include renewals in our bookings.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Okay. Is the sizing of it? Am I in the ballpark of? Because when I look -- and then I kind of run that going backwards, that number, typically, runs in the couple hundred million, plus or minus, seems a little bit larger this time? Was there any kind of large renewals, specifically? I think you mentioned one earlier. Is that what we're looking at here in this quarter?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

I think the increase, the biggest increase from last quarter, where we were at $4.1 billion or the $4.6 billion is really the inclusion of the EIS business into the base.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Okay, all right. Okay, that's helpful. If I look at just another question then on Practice Fusion. Can you -- you're adding Practice Fusion, another platform, you have actually Sunrise, TouchWorks, and I understand, I mean, you kind of run this sort of as a portfolio and give options to clients.

Can you talk about sort of your internal controls to manage sort of the different suites of products given the fact that it doesn't look like they are really looking to really integrate these into each other, right, but then would be kind of standalone offerings. Can you just talk about, like, how you're managing this and adding Practice Fusion to that? And also, what is sort of the support in terms of R&D? Do you think you got a need, not only just this year, but as we go over the next couple of years?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

So Charles, I'll take a shot. You had a lot of kind of sub-questions within that question, but let me take a shot. I mean, listen, as we've said several times, and I think I said earlier in the call, but I'll repeat it again. The market has very different and very real segments to it. And I'd say very real because, I mean, we didn't just invent this, you can see from behavior. I mean, there is a slew of healthcare providers, for instance, when you talk about Practice Fusion, who decided they want a very rudimentary tool, possibly just to pass Meaningful Use requirements, possibly just get out of paper, but they want a fairly rudimentary tool and in exchange for that, they paid very little, and they're okay with that. And you compare that to the other end of the market, where we have traditionally participated, where you have clients that are very complex clients that need sophisticated workflow, sophisticated content as part of their EHR. And as such, they're looking for something very different. So those market segments are real today. When you -- when any competitor, not just Allscripts, anybody thinks about addressing these different segments of the market, whether they've been in the ambulatory side or the inpatient, they have a choice to say, "Do I have this tool that's built for that market segment? Or do I try to dumb down a different tool that I already own or dumb up a different tool?" And our competitors have all taken different strategies. We don't believe in the dumbing-down strategy, we believe in offering a solution that was built for that market segment. So Practice Fusion is here to stay in our portfolio, it's built on modern technology platform, it's a single database, multi-tenant architected solution, efficient in that regard. And its R&D requirements are, what, modest, but certainly, are appropriate for the business and what we expect to generate from the business. So that's how we think about the portfolio of EHRs.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

I appreciate that. I guess, what I was really asking is, like, in terms of (inaudible) when all these units are reporting to you, your comfort in being able to manage another set of solutions as they kind of just -- are they are all kind of reporting to the same people? Just sort of more from an oversight perspective, that's all.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

So we have solution -- yes, we have solution leaders over -- all of our EHRs, each of our EHRs and their job is to really understand the requirements of its market segment and where the functionality is today, where it's going, what our competitors are doing, and they are tasked with building a solution road map. When we now -- I think maybe at the core of your questions, so how do we make sure those guys don't start stepping on each other's toes or overlapping. And yes, we do have a governance and control structure for that to ensure that the product roadmaps stay appropriate for the market segment that they're addressing.

Operator

Our next question comes from Stephanie Davis of Citi.

Stephanie July Davis - *Citigroup Inc, Research Division - VP & Senior Analyst*

Dennis, congrats on the new title.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Thanks, Stephanie.

Stephanie July Davis - *Citigroup Inc, Research Division - VP & Senior Analyst*

Just given the timing issue that you guys mentioned a little bit for bookings this quarter, could you talk to any potential pushouts that could impact the first half of '18? And just on that note, do you have any update on the timing of the Singapore EHR opportunity?

Paul Black

Yes, this is Paul. We have not yet been notified about Singapore. We expect something to be broadcast there this quarter. And then on the things that happened and didn't happen, I've said this in the past, and it's been something that has been kind of what happens in the real world, in every single quarter, there's a lot of deals that are there. If you look back to Q4 of 2016, there were four pretty good-sized deals that came in. And in this quarter, we didn't have those four deals. So that's part of the reasons why. Had we had those, we would have had another record. So on any given quarter, there could be one, two, three, four or five things that pushed out, that's just the reality of the world that we live in. We do everything we can possibly to bring -- and have that be consistent with the timing of the 90-day cycle, but it doesn't always work that way. When I look at 2018 in total, I see the pipeline, I see the teams, I see an energized EIS base, I see an energized EIS employee population. We had a really nice kick off when we brought some 700 people together and talked to them about what it's like to work at Allscripts, what our expectations are, what resources they have at their disposal. And you get a lot of people that were pretty excited about being part of an organization that just does healthcare information technology and services. So I'm not being overly buoyant about what's going to happen in any particular quarter, but as I look at over the balance of 2018, I feel confident that we'll continue to be successful in driving new business to the company as well as retaining clients as well as taking the new clients that we have that have not yet been exposed to the capabilities that Allscripts offers them. And our expectations there is pretty high with regard to the cross-selling of the solutions that we have into those bases.

Stephanie July Davis - *Citigroup Inc, Research Division - VP & Senior Analyst*

Good, understood. And one follow-up, and forgive me if I missed this. But can you just talk to the impact of tax or any below-the-line items in your '18 guidance? I'm just trying to reconcile the strength of the EBITDA guide compared to the EPS guide.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes, so the -- again, the effective tax rate that we're using for 2018 is 27%. That's really comprised of the federal, plus you add in state and some other penalties associated with being -- having some foreign entities that have profits attached to them. So that's the one big adjustment. Otherwise, everything is pretty much in line with (inaudible).

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

But I think if you're trying to square EBITDA to EPS, Stephanie, don't forget interest costs have gone up, and debt's gone up a bit and the cost of the money has gone up a little bit, too, with rising rates. So you need to check that in your model as well.

Paul Black

Well, thank you for your time today. As I mentioned earlier, Allscripts enters 2018 with top line growth, earnings momentum, strong financial capabilities and a good cash outlook. We are positioned for profitable growth. We appreciate your time, we appreciate your investment in Allscripts, and thank you very much.

Operator

This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation.