

COMPUTER PROGRAMS & SYSTEMS INC

Form 10-Q

August 08, 2017

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2017.

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to .

Commission file number: 000-49796

COMPUTER PROGRAMS AND SYSTEMS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware 74-3032373  
(State or Other Jurisdiction of (I.R.S. Employer  
Incorporation or Organization) Identification No.)

6600 Wall Street, Mobile, Alabama 36695  
(Address of Principal Executive Offices) (Zip Code)  
(251) 639-8100  
(Registrant's Telephone Number, Including Area Code)

N/A  
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of August 7, 2017, there were 13,755,726 shares of the issuer's common stock outstanding.

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COMPUTER PROGRAMS AND SYSTEMS, INC.

Quarterly Report on Form 10-Q

(For the three and six months ended June 30, 2017)

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## PART I

## FINANCIAL INFORMATION

## Item 1. Financial Statements.

## COMPUTER PROGRAMS AND SYSTEMS, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

(Unaudited)

	June 30, 2017	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,741	\$ 2,220
Accounts receivable, net of allowance for doubtful accounts of \$2,566 and \$2,370, respectively	34,655	31,812
Financing receivables, current portion, net	5,899	5,459
Inventories	1,075	1,697
Prepaid income taxes	758	567
Prepaid expenses and other	3,808	2,794
Total current assets	47,936	44,549
Property and equipment, net	12,485	13,439
Financing receivables, net of current portion	9,093	5,595
Intangible assets, net	101,915	107,118
Goodwill	168,449	168,449
Total assets	\$ 339,878	\$ 339,150
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 11,429	\$ 6,841
Current portion of long-term debt	7,389	5,817
Deferred revenue	8,564	5,840
Accrued vacation	4,604	3,650
Other accrued liabilities	10,079	8,797
Total current liabilities	42,065	30,945
Long-term debt, less current portion	136,011	146,989
Deferred tax liabilities	5,166	3,246
Total liabilities	183,242	181,180
Stockholders' equity:		
Common stock, \$0.001 par value; 30,000 shares authorized; 13,756 and 13,533 shares issued and outstanding	14	13
Additional paid-in capital	150,878	147,911
Retained earnings	5,744	10,046
Total stockholders' equity	156,636	157,970
Total liabilities and stockholders' equity	\$ 339,878	\$ 339,150

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of ContentsCOMPUTER PROGRAMS AND SYSTEMS, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Sales revenues:				
System sales and support	\$45,474	\$47,719	\$88,897	\$97,428
TruBridge	22,203	20,696	42,854	40,630
Total sales revenues	67,677	68,415	131,751	138,058
Costs of sales:				
System sales and support	18,859	21,886	37,789	44,153
TruBridge	11,933	11,616	23,520	22,903
Total costs of sales	30,792	33,502	61,309	67,056
Gross profit	36,885	34,913	70,442	71,002
Operating expenses:				
Product development	9,308	8,179	18,243	15,369
Sales and marketing	7,607	6,717	14,734	13,447
General and administrative	12,921	12,130	24,581	31,168
Amortization of acquisition-related intangibles	2,601	2,624	5,203	4,979
Total operating expenses	32,437	29,650	62,761	64,963
Operating income	4,448	5,263	7,681	6,039
Other income (expense):				
Other income	70	69	140	68
Interest expense	(1,938 )	(1,642 )	(3,745 )	(3,110 )
Total other income (expense)	(1,868 )	(1,573 )	(3,605 )	(3,042 )
Income before taxes	2,580	3,690	4,076	2,997
Provision for income taxes	993	1,694	2,243	2,664
Net income	\$1,587	\$1,996	\$1,833	\$333
Net income per common share—basic	\$0.11	\$0.15	\$0.13	\$0.03
Net income per common share—diluted	\$0.11	\$0.15	\$0.13	\$0.03
Weighted average shares outstanding used in per common share computations:				
Basic	13,420	13,317	13,397	13,171
Diluted	13,420	13,365	13,397	13,227
Dividends declared per common share	\$0.20	\$0.64	\$0.45	\$1.28

The accompanying notes are an integral part of these condensed consolidated financial statements.

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COMPUTER PROGRAMS AND SYSTEMS, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net income	\$1,587	\$1,996	\$1,833	\$333
Other comprehensive income, net of tax				
Change in unrealized income with realized income on the Statement of Income	—	6	—	38
Total other comprehensive income, net of tax	—	6	—	38
Comprehensive income	\$1,587	\$2,002	\$1,833	\$371

The accompanying notes are an integral part of these condensed consolidated financial statements.

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COMPUTER PROGRAMS AND SYSTEMS, INC.  
 CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY  
 (In thousands)  
 (Unaudited)

	Common Stock		Additional	Retained	Total
	Shares	Amount	Paid-in Capital	Earnings	Stockholders' Equity
Balance at December 31, 2016	13,533	\$ 13	\$147,911	\$10,046	\$ 157,970
Net income	—	—	—	1,833	1,833
Common stock issued upon exercise of stock options	—	—	1	—	1
Issuance of restricted stock	223	1	(1 )	—	—
Stock-based compensation	—	—	2,967	—	2,967
Dividends	—	—	—	(6,135 )	(6,135 )
Balance at June 30, 2017	13,756	\$ 14	\$150,878	\$5,744	\$ 156,636

The accompanying notes are an integral part of these condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Six Months Ended	
	June 30,	
	2017	2016
Operating Activities:		
Net income	1,833	\$333
Adjustments to net income:		
Provision for bad debt	473	451
Deferred taxes	1,920	1,748
Stock-based compensation	2,967	2,877
Excess tax benefit from stock-based compensation	—	(244 )
Depreciation	1,419	1,740
Amortization of acquisition-related intangibles	5,203	4,979
Amortization of deferred finance costs	365	330
Changes in operating assets and liabilities (net of acquired assets and liabilities):		
Accounts receivable	(3,013 )	(2,564 )
Financing receivables	(4,241 )	(574 )
Inventories	622	(10 )
Prepaid expenses and other	(1,014 )	242
Accounts payable	4,588	(4,260 )
Deferred revenue	2,724	(8,573 )
Other liabilities	2,236	(5,825 )
Prepaid income taxes/income taxes payable	(191 )	868
Net cash provided by (used in) operating activities	15,891	(8,482 )
Investing Activities:		
Purchases of property and equipment	(465 )	(39 )
Purchase of business, net of cash received	—	(162,611)
Sale of investments	—	10,861
Net cash used in investing activities	(465 )	(151,789)
Financing Activities:		
Dividends paid	(6,135 )	(17,244 )
Proceeds from long-term debt	—	156,572
Payments of long-term debt principal	(9,771 )	(1,562 )
Proceeds from exercise of stock options	1	1,134
Excess tax benefit from stock-based compensation	—	244
Net cash provided by (used in) financing activities	(15,905)	139,144
Decrease in cash and cash equivalents	(479 )	(21,127 )
Cash and cash equivalents at beginning of period	2,220	24,951
Cash and cash equivalents at end of period	\$1,741	\$3,824
Supplemental disclosure of cash flow information:		
Cash paid for interest	\$3,355	\$2,780
Cash paid for income taxes, net of refund	\$514	\$—
Supplemental disclosure of non-cash information:		
Fair value of common stock and options issued as consideration for acquisition of HHI	\$—	\$97,017
Write-off of fully depreciated assets	\$—	\$2,769



The accompanying notes are an integral part of these condensed consolidated financial statements.

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COMPUTER PROGRAMS AND SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. BASIS OF PRESENTATION

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") and include all adjustments that, in the opinion of management, are necessary for a fair presentation of the results of the periods presented. All such adjustments are considered of a normal recurring nature. Quarterly results of operations are not necessarily indicative of annual results.

Certain footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") have been condensed or omitted. The condensed consolidated balance sheet as of December 31, 2016 was derived from the audited consolidated balance sheet at that date. These unaudited condensed consolidated financial statements should be read in conjunction with the audited financial statements of Computer Programs and Systems, Inc. ("CPSI" or the "Company") for the year ended December 31, 2016 and the notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

Principles of Consolidation

The condensed consolidated financial statements of CPSI include the accounts of TruBridge, LLC ("TruBridge"), Evident, LLC ("Evident"), and Healthland Holding Inc. ("HHI"), all of which are wholly-owned subsidiaries of CPSI. The accounts of HHI include those of its wholly-owned subsidiaries, Healthland Inc. ("Healthland"), Rycan Technologies, Inc. ("Rycan"), and American HealthTech, Inc. ("AHT"). All significant intercompany balances and transactions have been eliminated.

Presentation

Effective January 1, 2017, we adopted a revised presentation of sales revenues and the associated costs of sales in our condensed consolidated statements of income, which we believe is better aligned with and representative of the amount and profitability of our revenue streams, as well as the way we manage our business, review our operating performance and market our products. Specifically:

The Company's sales revenues and costs of sales amounts formerly presented with the caption "Business management, consulting, and managed IT services" are now presented within the caption "TruBridge" within the condensed consolidated statements of income;

Rycan's sales revenues and costs of sales amounts formerly included within the caption "Systems sales and support" are now included within the caption "TruBridge" within the condensed consolidated statements of income;

Healthland and AHT revenues and costs of sales related to hosting services formerly included within the caption "Systems sales and support" are now included within the caption "TruBridge" within the condensed consolidated statements of income; and

- Certain Rycan expenses formerly included within the caption "General and administrative" are now included in cost of sales with the caption "TruBridge" within the condensed consolidated statements of income.

These reclassifications had no effect on previously reported total sales revenues, operating income, income before taxes or net income.

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Amounts presented for the three and six months ended June 30, 2016 have been reclassified to conform to the current presentation. The following table provides the amounts reclassified for the three months ended June 30, 2016:

(In thousands)	As previously reported	Reclassifications	As reclassified
Sales revenues:			
System sales	\$ 50,561	\$ (2,842 )	\$ 47,719
TruBridge	17,854	2,842	20,696
Costs of sales:			
System Sales	23,367	(1,481 )	21,886
TruBridge	9,913	1,703	11,616
Operating expenses:			
General and administrative	12,352	(222 )	12,130

The following table provides the amounts reclassified for the six months ended June 30, 2016:

(In thousands)	As previously reported	Reclassifications	As reclassified
Sales revenues:			
System sales	\$ 102,941	\$ (5,513 )	\$ 97,428
TruBridge	35,117	5,513	40,630
Costs of sales:			
System Sales	47,229	(3,076 )	44,153
TruBridge	19,440	3,463	22,903
Operating expenses:			
General and administrative	31,555	(387 )	31,168

## 2. BUSINESS COMBINATION

### Acquisition of HHI

On January 8, 2016, we acquired all of the assets and liabilities of HHI, including its wholly-owned subsidiaries, Healthland, AHT and Rycan. Healthland provides electronic health records ("EHR") and clinical information management solutions to over 350 hospital customers at the time of acquisition. AHT is a provider of clinical and financial solutions in the post-acute care market, serving over 3,300 skilled nursing facilities at the time of acquisition. Rycan offered SaaS-based revenue cycle management workflow and automation software to over 290 hospital customers at the time of acquisition.

We believe the acquisition of HHI:

- strengthened our position in providing healthcare information systems to community healthcare organizations with approximately 1,200 combined hospital customers at the time of acquisition;
- introduced CPSI to the post-acute care market; and
- expanded the products offered by and capabilities of TruBridge with the addition of Rycan and its suite of revenue cycle management software products.

These factors, combined with the synergies and economies of scale expected from combining the operations of CPSI and HHI, were the basis for the acquisition.

Consideration for the acquisition included cash (net of cash of the acquired entities) of \$162.6 million (inclusive of seller's transaction expenses), 1,973,880 shares of common stock of CPSI ("CPSI Common Stock"), and the assumption by CPSI of stock options that became exercisable for 174,972 shares of CPSI Common Stock. During the three and six months ended June 30, 2016, we incurred approximately \$0.5 million and \$8.0 million, respectively, of pre-tax acquisition costs in connection with the acquisition of HHI. Acquisition costs are included in general and administrative expenses in our condensed consolidated statements of income.



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(In thousands)	Purchase Price
Cash consideration, net of acquired cash received	\$ 162,611
Fair value of common stock and options issued as consideration	97,017
Total consideration	\$ 259,628

Our acquisition of HHI was treated as a purchase in accordance with Accounting Standards Codification (the "Codification") 805, Business Combinations, of the Financial Accounting Standards Board ("FASB"), which requires allocation of the purchase price to the estimated fair values of assets and liabilities acquired in the transaction. Our allocation of the purchase price was based on management's judgment after evaluating several factors, including a valuation assessment.

The allocation of the purchase price paid for HHI was as follows:

(In thousands)	Purchase Price Allocation
Acquired cash	\$ 5,371
Accounts receivable	5,789
Financing receivables	2,184
Inventories	216
Prepaid expenses	3,228
Property and equipment	1,263
Intangible assets	117,300
Goodwill	168,449
Accounts payable and accrued liabilities	(17,490 )
Deferred taxes, net	(4,010 )
Contingent consideration	(1,620 )
Deferred revenue	(15,681 )
Net assets acquired	\$ 264,999

The intangible assets in the table above are being amortized on a straight-line basis over their estimated useful lives. The amortization is included in amortization of acquisition-related intangibles in our condensed consolidated statements of income. Of the goodwill acquired, \$23.3 million is expected to be tax deductible.

The fair value measurements of tangible and intangible assets and liabilities were based on significant inputs not observable in the market and thus represent Level 3 measurements within the fair value measurement hierarchy (see Note 13). Level 3 inputs included, among others, discount rates that we estimated would be used by a market participant in valuing these assets and liabilities, projections of revenues and cash flows, client attrition rates and market comparables.

The gross contractual amount of accounts receivable of HHI at the date of acquisition was \$9.4 million.

### 3. REVENUE RECOGNITION

The Company recognizes revenue in accordance with U.S. GAAP, principally those required by the Software topic and Revenue Recognition subtopic of the FASB Codification and those prescribed by the SEC.

The Company's revenue is generated from two sources:

System Sales and Support - the sale of information systems and the provision of system support services. The sale of information systems includes perpetual software licenses, conversion, installation and training services, hardware and peripherals, "Software as a Service" (or "SaaS") services, and forms and supplies. System support services includes software application support, hardware maintenance, and continuing education.

TruBridge - the provision of business management services, which includes electronic billing, statement processing, payroll processing, accounts receivable management, contract management and insurance services, as



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well as Internet service provider ("ISP") services and consulting and managed IT services (collectively, "other professional IT services").

### System Sales and Support

The Company enters into contractual obligations to sell perpetual software licenses, conversion, installation and training services, hardware and software application support and hardware maintenance services. On average, the Company is able to complete a system installation in three to four weeks. The methods employed by the Company to recognize revenue, which are discussed by element below, achieve results materially consistent with the provisions of Accounting Standards Update ("ASU") 2009-13, Multiple-Deliverable Revenue Arrangements, due to the relatively short period during which there are multiple undelivered elements, the relatively small amount of non-software related elements in the system sale arrangements, and the limited number of contracts in-process at the end of each reporting period. The Company recognizes revenue on the elements noted above as follows:

**Perpetual software licenses and conversion, installation and training services** – The selling price of perpetual software licenses and conversion, installation and training services is based on management's best estimate of selling price. In determining management's best estimate of selling price, we consider the following: (1) competitor pricing, (2) supply and demand of installation staff, (3) overall economic conditions, and (4) our pricing practices as they relate to discounts. The method of recognizing revenue for the perpetual license of the associated modules included in the arrangement, and the related conversion, installation and training services over the term the services are performed, is on a module by module basis as the related perpetual licenses are delivered and the respective conversion, installation and training for each specific module is completed, as this is representative of the pattern of provision of these services.

**Hardware** – We recognize revenue for hardware upon shipment. The selling price of hardware is based on management's best estimate of selling price, which consists of cost plus a targeted margin.

**Software application support and hardware maintenance** – We have established vendor-specific objective evidence ("VSOE") of the fair value of our software application support and hardware maintenance services by reference to the price our customers are required to pay for the services when sold separately via renewals. Support and maintenance revenue is recognized on a straight-line basis over the term of the maintenance contract, which is generally three to five years.

**SaaS services** - The Company accounts for SaaS arrangements in accordance with the requirements of the Hosting Arrangement section under the Software topic and Revenue Recognition subtopic of the Codification. The Codification states that the software elements of SaaS services should not be accounted for as a hosting arrangement "if the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty and it is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software." Each SaaS contract entered into by the Company includes a system purchase and buyout clause, and this clause specifies the total amount of the system buyout. In addition, a clause is included in the contract which states that should the system be bought out by the customer, the customer would be required to enter into a general support agreement (for post-contract support services) for the remainder of the original SaaS term. Accordingly, the Company has concluded that SaaS customers do not have the right to take possession of the system without significant penalty (i.e., the purchase price of the system), resulting in the determination that these contracts are service contracts for which revenue is recognized when the services are performed.

### TruBridge

TruBridge consists of electronic billing, statement processing, payroll processing, accounts receivable management, contract management and insurance services. While TruBridge arrangements are contracts separate from the system sale and support contracts, these contracts are often executed within a short time frame of each other. The amount of the total arrangement consideration allocated to these services is based on VSOE of fair value by reference to the rate at which our customers renew as well as the rate at which the services are sold to customers when the TruBridge agreement is not executed within a short time frame of the system sale and support contracts. If VSOE of fair value does not exist for these services, we allocate arrangement consideration based on third-party evidence ("TPE") of selling price or, if neither VSOE nor TPE is available, estimated selling price. Because the pricing is transaction based

(per unit pricing), customers are billed and revenue recognized as services are performed based on transaction levels. The Company will occasionally provide ISP and other professional IT services. Depending on the nature of the services provided, these services may be considered software elements or non-software elements. The selling price of services



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considered to be software elements is based on VSOE of the fair value of the services by reference to the price our customers are required to pay for the services when sold separately. The selling price of services considered to be non-software elements is based on third-party evidence of selling price of similar services. Revenue from these elements is recognized as the services are performed.

#### 4. PROPERTY AND EQUIPMENT

Property and equipment were comprised of the following at June 30, 2017 and December 31, 2016:

(In thousands)	June 30, 2017	December 31, 2016
Land	\$2,848	\$ 2,848
Buildings and improvements	9,432	9,432
Maintenance equipment	802	802
Computer equipment	5,639	5,174
Leasehold improvements	5,007	5,007
Office furniture and fixtures	3,591	3,591
Automobiles	335	335
	27,654	27,189
Less: accumulated depreciation (15,169 )	(13,750 )	
Property and equipment, net	\$12,485	\$ 13,439

#### 5. OTHER ACCRUED LIABILITIES

Other accrued liabilities were comprised of the following at June 30, 2017 and December 31, 2016:

(In thousands)	June 30, 2017	December 31, 2016
Salaries and benefits	\$4,098	\$ 5,397
Severance	2,129	337
Commissions	1,082	518
Self-insurance reserves	1,029	887
Contingent consideration	1,120	1,120
Other	621	538
	\$10,079	\$ 8,797

The accrued contingent consideration depicted above represents the potential earnout incentive for former Rycan shareholders. We have estimated the fair value of the contingent consideration based on the amount of revenue we expect to be earned by Rycan through the year ending December 31, 2018.

#### 6. NET INCOME PER SHARE

The Company presents basic and diluted earnings per share ("EPS") data for its common stock. Basic EPS is calculated by dividing the net income attributable to stockholders of the Company by the weighted average number of shares of common stock outstanding during the period. Diluted EPS is determined by adjusting the net income attributable to stockholders of the Company and the weighted average number of shares of common stock outstanding during the period for the effects of all dilutive potential common shares, including awards under stock-based compensation arrangements.

The Company's unvested restricted stock awards (see Note 8) are considered participating securities under FASB Codification topic, Earnings Per Share, because they entitle holders to non-forfeitable rights to dividends until the awards vest or are forfeited. When a company has a security that qualifies as a "participating security," the Codification requires the use of the two-class method when computing basic EPS. The two-class method is an earnings allocation formula that determines EPS for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. In determining the amount of net income to allocate to common stockholders, income is allocated to both common stock and participating securities based on their respective weighted average shares outstanding for the period, with net income attributable to common stockholders ultimately



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equaling net income less net income attributable to participating securities. Diluted EPS for the Company's common stock is computed using the more dilutive of the two-class method or the treasury stock method.

The following is a calculation of the basic and diluted EPS for the Company's common stock, including a reconciliation between net income and net income attributable to common stockholders:

	Three Months		Six Months	
	Ended	Ended	Ended	Ended
(in thousands, except per share data)	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Net income	\$1,587	\$1,996	\$1,833	\$ 333
Less: Net (income) loss attributable to participating securities	(45 )	(32 )	(41 )	15
Net income attributable to common stockholders	\$1,542	\$1,964	\$1,792	\$ 348
Weighted average shares outstanding used in basic per common share computations	13,420	13,317	13,397	13,171
Add: Dilutive potential common shares	—	48	—	56
Weighted average shares outstanding used in diluted per common share computations	13,420	13,365	13,397	13,227
Basic EPS	\$0.11	\$0.15	\$0.13	\$ 0.03
Diluted EPS	\$0.11	\$0.15	\$0.13	\$ 0.03

During 2017, performance share awards were granted to certain executive officers and key employees of the Company that will result in the issuance of time-vesting restricted stock if the predefined performance criteria are met. The awards provide for an aggregate target of 189,325 shares, none of which have been included in the calculation of diluted EPS for the three and six months ended June 30, 2017 because the related threshold award performance level has not been achieved as of June 30, 2017. See Note 8.

## 7. INCOME TAXES

The Company determines the tax provision for interim periods using an estimate of our annual effective tax rate, adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter we update our estimate of the annual effective tax rate, and if our estimated tax rate changes, we make a cumulative adjustment. Our effective tax rate for the three months ended June 30, 2017 decreased to 38.5% from 45.9% for the three months ended June 30, 2016. During the three months ended June 30, 2016 the identification of nondeductible facilitative transaction costs and adjustments in our estimated state effective tax rate resulted in combined additional income tax expense of \$0.4 million, increasing the period's effective tax rate by 11.2%. Conversely, during the three months ended June 30, 2017 we experienced a shortfall tax expense related to restricted stock of \$0.2 million that increased the effective rate by 6.1% due to the adoption of ASU 2016-09 as detailed in Note 15.

Our effective tax rate for the six months ended June 30, 2017 decreased to 55.0% compared to 88.9% for the six months ended June 30, 2016. During the six months ended June 30, 2016 the identification of nondeductible facilitative transaction costs resulted in additional income tax expense of \$1.4 million, increasing the period's effective tax rate by 49.1%. Conversely, during the six months ended June 30, 2017 we experienced a shortfall tax expense related to restricted stock of \$0.9 million that increased the effective tax rate by 22.6% due to the adoption of ASU 2016-09 as detailed in Note 15.

## 8. STOCK-BASED COMPENSATION

Stock-based compensation cost is measured at the grant date based on the fair value of the award, and is recognized as an expense over the employee's or non-employee director's requisite service period.

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The following table details total stock-based compensation expense for the three and six months ended June 30, 2017 and 2016, included in the condensed consolidated statements of income:

(In thousands)	Three Months Ended		Six Months Ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Costs of sales	\$425	\$374	\$743	\$773
Operating expenses	1,261	1,120	2,224	2,104
Pre-tax stock-based compensation expense	1,686	1,494	2,967	2,877
Less: income tax effect	(658 )	(583 )	(1,157 )	(1,122 )
Net stock-based compensation expense	\$1,028	\$911	\$1,810	\$1,755

The Company's stock-based compensation awards are in the form of restricted stock and performance share awards made pursuant to the Company's 2005 Restricted Stock Plan, 2012 Restricted Stock Plan for Non-Employee Directors, and the Amended and Restated 2014 Incentive Plan (the "Plans"). As of June 30, 2017, there was \$14.1 million of unrecognized compensation cost related to non-vested stock-based compensation arrangements granted under the Plans, which is expected to be recognized over a weighted-average period of 2.4 years.

**Restricted Stock**

The Company grants restricted stock to executive officers, certain key employees and non-employee directors under the Plans with the fair value of the awards representing the fair value of the common stock on the date the restricted stock is granted. Shares of restricted stock generally vest in equal annual installments over the applicable vesting period, which ranges from one to five years. The Company records expenses for these grants on a straight-line basis over the applicable vesting periods. Shares of restricted stock may also be issued pursuant to the settlement of performance share awards, for which the Company records expenses in the manner described in the "Performance Share Awards" section below.

A summary of restricted stock activity (including shares of restricted stock issued pursuant to the settlement of performance share awards) under the Plans during the six months ended June 30, 2017 and 2016 is as follows:

	Six Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	Shares	Weighted-Average Grant Date Fair Value Per Share	Shares	Weighted-Average Grant Date Fair Value Per Share
Nonvested restricted stock outstanding at beginning of period	184,885	\$ 54.63	191,397	\$ 57.12
Granted	222,390	32.87	86,984	52.21
Vested	(80,558 )	55.34	(72,393 )	57.75
Nonvested restricted stock outstanding at end of period	326,717	\$ 39.64	205,988	\$ 54.82

**Performance Share Awards**

In 2014, the Company began to grant performance share awards to executive officers and certain key employees under the Amended and Restated 2014 Incentive Plan ("2014 Incentive Plan"). The number of shares of common stock earned and issuable under the award is determined at the end of each performance period, based on the Company's achievement of performance goals predetermined by the Compensation Committee of the Board of Directors at the time of grant. If certain levels of the performance objective are met, the award results in the issuance of shares of restricted stock corresponding to such level, which shares are then subject to time-based vesting pursuant to which the shares of restricted stock vest in equal annual installments over the applicable vesting period, which is generally three years for restricted stock issued pursuant to performance share awards.



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In the event that the Company's financial performance meets the predetermined target for the performance objective, the Company will issue each award recipient the number of restricted shares equal to the target award specified in the individual's underlying performance share award agreement. In the event the financial results of the Company exceed the predetermined target, additional shares up to the maximum award may be issued. In the event the financial results of the Company fall below the predetermined target, a reduced number of shares may be issued. If the financial results of the Company fall below the threshold performance level, no shares will be issued.

The recipients of performance share awards do not receive dividends or possess voting rights during the performance period and, accordingly, the fair value of the performance share awards is the quoted market value of CPSI Common Stock on the grant date less the present value of the expected dividends not received during the relevant period.

Expense is recognized using the accelerated attribution (graded vesting) method over the period beginning on the date the Company determines that it is probable that the performance criteria will be achieved and ending on the last day of the vesting period for the restricted stock issued in satisfaction of such awards. In the event the Company determines it is no longer probable that the minimum performance level will be achieved, all previously recognized compensation expense related to the applicable awards is reversed in the period such a determination is made.

A summary of performance share award activity under the 2014 Incentive Plan during the six months ended June 30, 2017 and 2016 is as follows, based on the target award amounts set forth in the performance share award agreements:

	Six Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	Shares	Weighted-Average Grant Date Fair Value	Shares	Weighted-Average Grant Date Fair Value
Performance share awards outstanding at beginning of period	77,594	\$ 49.64	49,471	\$ 49.29
Granted	189,325	29.94	77,594	49.64
Forfeited or unearned	(77,594 )	49.64	(49,471 )	49.29
Performance share awards outstanding at end of period	189,325	\$ 29.94	77,594	\$ 49.64

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## 9. FINANCING RECEIVABLES

## Short-Term Payment Plans

The Company has sold information and patient care systems to certain healthcare providers under Second Generation Meaningful Use Installment Plans (see below) with maximum contractual terms of three years and expected terms of less than one year and other arrangements requiring fixed monthly payments over terms ranging from three to 12 months ("Fixed Periodic Payment Plans"). These receivables, collectively referred to as short-term payment plans and included in the current portion of financing receivables, were comprised of the following at June 30, 2017 and December 31, 2016:

(In thousands)	June 30, December 31,	
	2017	2016
Second Generation Meaningful Use Installment Plans, gross	\$320	\$ 3,080
Fixed Periodic Payment Plans, gross	1,384	1,988
Short-term payment plans, gross	\$1,704	\$ 5,068
Less: allowance for losses	(317 )	(1,796 )
Short-term payment plans, net	\$1,387	\$ 3,272

## Sales-Type Leases

Additionally, the Company leases its information and patient care systems to certain healthcare providers under sales-type leases expiring in various years through 2024. These receivables typically have terms from two to seven years, bear interest at various rates, and are usually collateralized by a security interest in the underlying assets. Since the Company has a history of successfully collecting amounts due under the original payment terms of these extended payment arrangements without making any concessions to its customers, the Company satisfies the requirement for revenue recognition. The Company's history with these types of extended payment term arrangements supports management's assertion that revenues are fixed and determinable and collection is probable.

The components of these lease receivables were as follows at June 30, 2017 and December 31, 2016:

(In thousands)	June 30, December 31,	
	2017	2016
Sales-type leases, gross	\$16,727	\$ 8,981
Less: allowance for losses	(1,612 )	(402 )
Less: unearned income	(1,510 )	(797 )
Sales-type leases, net	\$13,605	\$ 7,782

Future minimum lease payments to be received subsequent to June 30, 2017 are as follows:

(In thousands)

Years Ended December 31,	
2017	\$3,001
2018	4,071
2019	3,398
2020	2,914
2021	2,123
Thereafter	1,220
Total minimum lease payments to be received	16,727
Less: allowance for losses	(1,612 )
Less: unearned income	(1,510 )
Lease receivables, net	\$13,605





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## Credit Quality of Financing Receivables and Allowance for Credit Losses

The following table is a roll-forward of the allowance for financing credit losses for the six months ended June 30, 2017 and year ended December 31, 2016:

(In thousands)	Balance at Beginning of Period	Provision	Charge-offs	Recoveries	Balance at End of Period
June 30, 2017	\$ 2,198	\$ 303	\$ (572 )	\$	—\$ 1,929
December 31, 2016	\$ 654	\$ 1,762	\$ (218 )	\$	—\$ 2,198

The Company's financing receivables are comprised of a single portfolio segment, as the balances are all derived from short-term payment plan arrangements and sales-type leasing arrangements within our target market of rural and community hospitals. The Company evaluates the credit quality of its financing receivables based on a combination of factors, including, but not limited to, customer collection experience, economic conditions, the customer's financial condition, and known risk characteristics impacting the respective customer base of rural and community hospitals, the most notable of which relate to enacted and potential changes in Medicare and Medicaid reimbursement rates as rural and community hospitals typically generate a significant portion of their revenues and related cash flows from beneficiaries of these programs. In addition to specific account identification, the Company utilizes historical collection experience to establish the allowance for credit losses. Financing receivables are written off only after the Company has exhausted all collection efforts. The Company has been successful in collecting its financing receivables and considers the credit quality of such arrangements to be good, especially as the underlying assets act as collateral for the receivables.

Customer payments are considered past due if a scheduled payment is not received within contractually agreed upon terms. To facilitate customer collection and credit monitoring efforts, financing receivable amounts are invoiced and reclassified to trade accounts receivable when they become due, with all invoiced amounts placed on nonaccrual status. As a result, all past due amounts related to the Company's financing receivables are included in trade accounts receivable in the accompanying condensed consolidated balance sheets. The following is an analysis of the age of financing receivables amounts (excluding short-term payment plans) that have been reclassified to trade accounts receivable and were past due as of June 30, 2017 and December 31, 2016:

(In thousands)	1 to 90 Days Past Due	91 to 180 Days Past Due	181 + Days Past Due	Total Past Due
June 30, 2017	\$ 384	\$ 33	\$ 42	\$ 459
December 31, 2016	\$ 228	\$ 31	\$ 34	\$ 293

From time to time, the Company may agree to alternative payment terms outside of the terms of the original financing receivable agreement due to customer difficulties in achieving the original terms. In general, such alternative payment arrangements do not result in a re-aging of the related receivables. Rather, payments pursuant to any alternative payment arrangements are applied to the already outstanding invoices beginning with the oldest outstanding invoices as the payments are received.

Because amounts are reclassified to trade accounts receivable when they become due, there are no past due amounts included within financing receivables or the financing receivables, current portion, net amount in the accompanying condensed consolidated balance sheets.

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The Company utilizes an aging of trade accounts receivable as the primary credit quality indicator for its financing receivables, which is facilitated by the reclassification of customer payment amounts to trade accounts receivable when they become due. The table below categorizes customer financing receivable balances (excluding short-term payment plans), none of which are considered past due, based on the age of the oldest payment outstanding that has been reclassified to trade accounts receivable:

(In thousands)	June 30, 2017	December 31, 2016
Customer balances with amounts reclassified to trade accounts receivable that are:		
1 to 90 Days Past Due	\$8,632	\$ 6,167
91 to 180 Days Past Due	1,511	550
181 + Days Past Due	827	273
Total customer balances with past due amounts reclassified to trade accounts receivable	\$10,970	\$ 6,990
Total customer balances with no past due amounts reclassified to trade accounts receivable	4,247	1,194
Total financing receivables with contractual maturities of one year or less	1,704	5,068
Less: allowance for losses	(1,929 )	(2,198 )
Total financing receivables	\$14,992	\$ 11,054

**Second Generation Meaningful Use Installment Plans**

Beginning in the fourth quarter of 2012, we offered to our customers license agreements with payment terms that provided us with greater visibility into and control over the customer's meaningful use attestation process and significantly reduced the maximum timeframe over which customers must satisfy their full payment obligations in purchasing our system ("Second Generation Meaningful Use Installment Plans"). As the overall payment period durations of the Second Generation Meaningful Use Installment Plans are consistent with that of our historical system sale financing arrangements, revenues under the Second Generation Meaningful Use Installment Plans are recognized upon installation of our EHR solution. Although these arrangements provide for a maximum payment term of three years, management has determined the expected term for these arrangements to be less than one year due to (a) historical collection patterns of required EHR incentive payment amounts and (b) the estimated significance of those amounts, the receipt of which is expected to result in minimal or no remaining balance for the related arrangements. As a result, all related amounts are included as a component of financing receivables, current portion, net in the accompanying condensed consolidated balance sheets and as a component of short-term payment plans within this note.

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## 10. INTANGIBLE ASSETS AND GOODWILL

Our purchased definite-lived intangible assets as of June 30, 2017 are summarized as follows:

(In thousands)	Customer Relationships	Trademark	Developed Technology	Total
Gross carrying amount	\$ 82,300	\$ 10,900	\$ 24,100	\$ 117,300
Accumulated amortization	(9,668 )	(1,257 )	(4,460 )	(15,385 )
Net intangible assets	\$ 72,632	\$ 9,643	\$ 19,640	\$ 101,915
Weighted average remaining years of useful life	11	14	7	11

The following table represents the remaining amortization of definite-lived intangible assets as of June 30, 2017:

(In thousands)

For the year ended December 31,

2017	\$5,202
2018	10,406
2019	10,112
2020	10,106
2021	10,066
Due thereafter	56,023
Total	\$ 101,915

The following table sets forth the change in the carrying amount of goodwill by segment for the six months ended June 30, 2017:

(In thousands)	Acute Care EHR	Post-acute Care EHR	TruBridge	Total
Balance as of December 31, 2016	\$97,095	\$ 57,570	\$ 13,784	\$ 168,449
Goodwill acquired	—	—	—	—
Balance as of June 30, 2017	\$97,095	\$ 57,570	\$ 13,784	\$ 168,449

Goodwill is evaluated for impairment annually on October 1, or more frequently if indicators of impairment are present or changes in circumstances suggest that impairment may exist. As of June 30, 2017, there was no impairment to goodwill.

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## 11. LONG-TERM DEBT

Long-term debt was comprised of the following at June 30, 2017 and December 31, 2016:

(In thousands)	June 30, 2017	December 31, 2016
Term loan facility	\$ 118,750	\$ 121,875
Revolving credit facility	26,500	33,000
Capital lease obligation	716	861
Debt obligations	145,966	155,736
Less: unamortized debt issuance costs	(2,566 )	(2,930 )
Debt obligation, net	143,400	152,806
Less: current portion	(7,389 )	(5,817 )
Long-term debt	\$ 136,011	\$ 146,989

As of June 30, 2017, the carrying value of debt approximates the fair value due to the variable interest rate.

Credit Agreement

In conjunction with our acquisition of HHI on January 8, 2016, we entered into a syndicated credit agreement on the same date (the "Credit Agreement"), with Regions Bank ("Regions") serving as administrative agent, which provided for a \$125,000,000 term loan facility (the "Term Loan Facility") and a \$50,000,000 revolving credit facility ("Revolving Credit Facility"). The cash portion of the purchase price for HHI was partially funded by the \$125,000,000 Term Loan Facility and \$25,000,000 borrowed under the Revolving Credit Facility.

The Term Loan Facility bears interest at a rate per annum equal to an applicable margin plus (1) the Adjusted LIBOR rate for the relevant interest period, (2) an alternate base rate determined by reference to the greater of (a) the prime lending rate of Regions, (b) the federal funds rate for the relevant interest period plus one half of one percent per annum and (c) the one-month LIBOR rate plus one percent per annum, or (3) a combination of (1) and (2). Interest on the outstanding principal of the Term Loan Facility is payable on the last day of each month, in the case of each base rate loan, and on the last day of each interest period (but no less frequently than every three months), in the case of LIBOR loans. Principal payments are due on the last day of each fiscal quarter beginning March 31, 2016, with the remainder due at maturity on January 8, 2021 (the "Maturity Date"). Anticipated annual future maturities of the Term Loan Facility, Revolving Credit Facility, and capital lease obligation are as follows as of June 30, 2017:

(In thousands)	
2017	\$ 3,276
2018	9,690
2019	12,750
2020	15,625
2021	104,625
Thereafter	—
	\$ 145,966

Borrowings under the Revolving Credit Facility bear interest at a rate similar to that of the Term Loan Facility, with interest payment dates similar to that of the Term Loan Facility. The Revolving Credit Facility includes a \$5 million swingline sublimit, with swingline loans bearing interest at the alternate base rate plus the applicable margin. Any principal outstanding under the Revolving Credit Facility is due and payable on the Maturity Date.

The Term Loan Facility and amounts borrowed under the Revolving Credit Facility are secured pursuant to a Pledge and Security Agreement, dated January 8, 2016, among the parties identified as Obligors therein and Regions, as collateral agent (the "Security Agreement"), on a first priority basis by a security interest in substantially all of the tangible and intangible assets (subject to certain exceptions) of the Company and certain subsidiaries of the Company, as guarantors (collectively, the "Subsidiary Guarantors"), including certain registered intellectual property and the capital stock of certain

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of the Company's direct and indirect subsidiaries. Our obligations under the Credit Agreement are also guaranteed by the Subsidiary Guarantors.

The Credit Agreement provides incremental facility capacity of \$50 million, subject to certain conditions. The Credit Agreement includes a number of restrictive covenants that, among other things and in each case subject to certain exceptions and baskets, impose operating and financial restrictions on the Company and the Subsidiary Guarantors, including the ability to incur additional debt; incur liens and encumbrances; make certain restricted payments, including paying dividends on its equity securities or payments to redeem, repurchase or retire its equity securities; enter into certain restrictive agreements; make investments, loans and acquisitions; merge or consolidate with any other entity; dispose of assets; enter into sale and leaseback transactions; engage in transactions with its affiliates; and materially alter the business it conducts. In addition, the Company is required to comply with a minimum fixed charge coverage ratio throughout the duration of the Credit Agreement and a maximum consolidated leverage ratio. The Credit Agreement also contains customary representations and warranties, affirmative covenants and events of default. The Credit Agreement requires the Company to mandatorily prepay the Term Loan Facility and amounts borrowed under the Revolving Credit Facility with (i) 100% of net cash proceeds from certain sales and dispositions, subject to certain reinvestment rights, (ii) 100% of net cash proceeds from certain issuances or incurrences of additional debt, (iii) 50% of net cash proceeds from certain issuances or sales of equity securities, subject to a step down to 0% if the Company's consolidated leverage ratio is no greater than 2.50:1.0, and (iv) beginning with the fiscal year ending December 31, 2016, 50% of excess cash flow (minus certain specified other payments), subject to a step down to 0% of excess cash flow if the Company's consolidated leverage ratio is no greater than 2.50:1.0. The Company is permitted to voluntarily prepay the Term Loan Facility and amounts borrowed under the Revolving Credit Facility at any time without penalty, subject to customary "breakage" costs with respect to prepayments of LIBOR rate loans made on a day other than the last day of any applicable interest period. As of June 30, 2017, we believe that we were in compliance with all debt covenants contained in the Credit Agreement.

12. COMMITMENTS AND CONTINGENCIES

From time to time, the Company is involved in routine litigation that arises in the ordinary course of business. Management does not believe it is reasonably possible that such matters will have a material adverse effect on the Company's financial statements.

13. FAIR VALUE

FASB Codification topic, Fair Value Measurements and Disclosures, establishes a framework for measuring fair value and expands financial statement disclosures about fair value measurements. Fair value is the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. The Codification does not require any new fair value measurements, but rather applies to all other accounting pronouncements that require or permit fair value measurements. The Codification requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market-based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

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The accrued contingent consideration depicted below represents the potential earnout incentive for former Rycan shareholders, relating to the purchase of Rycan by HHI in 2015. We have estimated the fair value of the contingent consideration based on the amount of revenue we expect to be earned by Rycan through the year ending December 31, 2018.

The following table summarizes the carrying amounts and fair values of certain liabilities at June 30, 2017:

Description	Carrying Amount at 6/30/2017	Fair Value at June 30, 2017	
		Using Quoted Prices in Significant Other Observable Inputs for Identical Assets (Level 1)	Using Significant Unobservable Inputs (Level 2) (Level 3)
Contingent consideration	\$ 1,120	\$—	—\$ 1,120
Total	\$ 1,120	\$—	—\$ 1,120

The following table summarizes the carrying amounts and fair values of certain liabilities at December 31, 2016:

Description	Carrying Amount at 12/31/2016	Fair Value at December 31, 2016	
		Using Quoted Prices in Significant Other Observable Inputs for Identical Assets (Level 1)	Using Significant Unobservable Inputs (Level 2) (Level 3)
Contingent consideration	\$ 1,120	\$—	—\$ 1,120
Total	\$ 1,120	\$—	—\$ 1,120

The carrying amounts of other financial instruments reported in the consolidated balance sheets for current assets and current liabilities approximate their fair values because of the short-term nature of these instruments.

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## 14. SEGMENT REPORTING

Our chief operating decision makers ("CODM") utilize three operating segments, "Acute Care EHR", "Post-acute Care EHR" and "TruBridge", based on our three distinct business units with unique market dynamics and opportunities. Revenues and cost of sales are primarily derived from the provision of services and sales of our proprietary software, and our CODM assess the performance of these three segments at the gross profit level. Operating expenses and items such as interest, income tax, capital expenditures and total assets are managed at a consolidated level and thus are not included in our operating segment disclosures. Our CODM group is comprised of the Chief Executive Officer, Chief Growth Officer, Chief Operating Officer, and Chief Financial Officer. Accounting policies for each of the reportable segments are the same as those used on a consolidated basis.

As of January 1, 2017, the operating segment formerly identified as "TruBridge, Rycan, and Other Outsourcing" is now identified as "TruBridge".

The following table presents a summary of the revenues and gross profits of our three operating segments for the three and six months ended June 30, 2017 and 2016:

(In thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
<b>Revenues:</b>				
Acute Care EHR	\$39,394	\$40,754	\$76,525	\$83,494
Post-acute Care EHR	6,080	6,965	12,372	13,934
TruBridge	22,203	20,696	42,854	40,630
Total revenues	\$67,677	\$68,415	\$131,751	\$138,058
<b>Cost of sales:</b>				
Acute Care EHR	\$16,836	\$19,364	33,753	39,250
Post-acute Care EHR	2,023	2,522	4,036	4,903
TruBridge	11,933	11,616	23,520	22,903
Total cost of sales	\$30,792	\$33,502	\$61,309	\$67,056
<b>Gross profit:</b>				
Acute Care EHR	\$22,558	\$21,390	42,772	44,244
Post-acute Care EHR	4,057	4,443	8,336	9,031
TruBridge	10,270	9,080	19,334	17,727
Total gross profit	\$36,885	\$34,913	\$70,442	\$71,002
Corporate operating expenses	\$(32,437)	(29,650)	(62,761)	(64,963)
Other income	70	69	140	68
Interest expense	(1,938)	(1,642)	(3,745)	(3,110)
Income before taxes	\$2,580	\$3,690	\$4,076	\$2,997

## 15. RECENT ACCOUNTING PRONOUNCEMENTS

## New Accounting Standards Adopted in 2017

In July 2015, the FASB issued ASU 2015-11, Simplifying the Measurement of Inventory. The amended guidance requires entities to measure inventory at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The requirement would replace the current lower of cost or market evaluation. Accounting guidance is unchanged for inventory measured using last-in, first-out ("LIFO") or the retail method. The amended guidance will be effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15,





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2017. The amended guidance should be applied prospectively with earlier application permitted. The adoption of ASU 2015-11 did not have a material effect on our financial statements.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting, which simplifies the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and the classification of awards on the statement of cash flows. This guidance will be effective for fiscal years and interim periods within those years beginning after December 15, 2016, which is effective for the Company as of the first quarter of our fiscal year ending December 31, 2017. The adoption of ASU 2016-09 had a material effect on our financial statements in the period of adoption and is disclosed in Note 7 of the financial statements.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment, that removes step two of the goodwill impairment test, which requires a hypothetical purchase price allocation. Under the new guidance, a goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. All other goodwill impairment guidance will remain largely unchanged. Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. The guidance is effective for annual and interim periods in fiscal years beginning after December 15, 2019 with early adoption permitted for any goodwill impairment tests performed after January 1, 2017. The guidance is to be applied prospectively.

We have elected to early adopt ASU 2017-04 and the guidance will be applied for all goodwill impairment tests performed after January 1, 2017. The adoption of ASU 2017-04 may have a material impact on our financial statements if one or more of our reporting unit's carrying value exceeds its fair value at the time of impairment assessment.

**New Accounting Standards Yet to be Adopted**

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards. The standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes the most current revenue recognition guidance. This guidance will be effective for fiscal years and interim periods within those years beginning after December 15, 2017, which is effective for the Company as of the first quarter of our fiscal year ending December 31, 2018. Although we have not fully completed the assessment of our systems, data, and processes that will be affected by the implementation of this standard, we currently anticipate that this standard will not significantly alter revenue recognition practices for our system sales and support and TruBridges revenue streams but may have a material impact on our consolidated financial statements with respect to the capitalization of certain commissions and contract fulfillment costs which are currently expensed as incurred. We intend to adopt this standard using the modified retrospective method, in which the cumulative effect of initially applying the guidance will be recognized as an adjustment to retained earnings or impacted balance sheet line items as of January 1, 2018, the date of adoption.

In February 2016, the FASB issued ASU 2016-02, Leases, to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The new guidance will require the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous U.S. GAAP. This guidance will be effective for fiscal years and interim periods within those years beginning after December 15, 2018, which is effective for the Company as of the first quarter of our fiscal year ending December 31, 2019. The Company is currently evaluating the impact that the implementation of this standard will have on its financial statements.

In August 2016, the FASB issued ASU 2016-15, Classifications of Certain Cash Receipts and Cash Payments, which clarifies cash flow classification for eight specific issues, including debt prepayment or extinguishment costs,

contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, and proceeds from settlement of corporate-owned life insurance policies. This guidance will be effective for fiscal years and interim periods within those years beginning after December 15, 2017, which is effective for the Company as of the first quarter of our fiscal year ending December 31, 2018. The Company is currently evaluating the impact that the implementation of this standard will have on its financial statements.

In January 2017, the FASB issued ASU 2017-01, Clarifying the Definition of a Business, to assist an entity in evaluating when a set of transferred assets and activities is a business. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017 and should be applied prospectively to any transactions occurring within the period of adoption. Early adoption is permitted, including for interim or annual periods in which the

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financial statements have not been issued or made available for issuance. The Company is currently evaluating the impact that the implementation of this standard will have on its financial statements.

We do not believe that any other recently issued, but not yet effective accounting standards, if adopted, would have a material impact on our consolidated financial statements.

16. SUBSEQUENT EVENTS

On August 3, 2017, the Company announced a dividend for the third quarter of 2017 in the amount of \$0.30 per share, payable on September 1, 2017, to stockholders of record as of the close of business on August 17, 2017.

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

You should read the following discussion and analysis of our financial condition and results of operations together with the unaudited condensed consolidated financial statements and related notes appearing elsewhere herein.

This discussion and analysis contains forward-looking statements within the meaning of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified generally by the use of forward-looking terminology and words such as "expects," "anticipates," "estimates," "believes," "predicts," "intends," "plans," "potential," "may," "continue," "should," "will" and words of comparable meaning.

Without limiting the generality of the preceding statement, all statements in this report relating to estimated and projected earnings, margins, costs, expenditures, cash flows, growth rates and future financial results are forward-looking statements. We caution investors that any such forward-looking statements are only predictions and are not guarantees of future performance. Certain risks, uncertainties and other factors may cause actual results to differ materially from those projected in the forward-looking statements. Such factors may include:

- overall business and economic conditions affecting the healthcare industry, including the potential effects of the federal healthcare reform legislation enacted in 2010, and implementing regulations, on the businesses of our hospital customers;

- government regulation of our products and services and the healthcare and health insurance industries, including changes in healthcare policy affecting Medicare and Medicaid reimbursement rates and qualifying technological standards;

- changes in customer purchasing priorities, capital expenditures and demand for information technology systems;

- saturation of our target market and hospital consolidations;

- general economic conditions, including changes in the financial and credit markets that may affect the availability and cost of credit to us or our customers;

- our substantial indebtedness, and our ability to incur additional indebtedness in the future;

- our potential inability to generate sufficient cash in order to meet our debt service obligations;

- restrictions on our current and future operations because of the terms of our senior secured credit facilities;

- market risks related to interest rate changes;

- our ability to successfully integrate the businesses of Healthland Inc., American HealthTech, Inc., and Rycan Technologies, Inc. with our business and the inherent risks associated with any potential future acquisitions;

- our ability to remediate a material weakness in our internal control over financial reporting;

- competition with companies that have greater financial, technical and marketing resources than we have;

- failure to develop new or enhance current technology and products in response to market demands;

- failure of our products to function properly resulting in claims for losses;

- breaches of security and viruses in our systems resulting in customer claims against us and harm to our reputation;

- failure to maintain customer satisfaction through new product releases or enhancements free of undetected errors or problems;

- interruptions in our power supply and/or telecommunications capabilities, including those caused by natural disaster;

- our ability to attract and retain qualified and key personnel;

- failure to properly manage growth in new markets we may enter;

- misappropriation of our intellectual property rights and potential intellectual property claims and litigation against us;

- changes in accounting principles generally accepted in the United States of America;

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significant charge to earnings if our goodwill or intangible assets become impaired; and fluctuations in quarterly financial performance due to, among other factors, timing of customer installations. Additional information concerning these and other factors that could cause differences between forward-looking statements and future actual results is discussed under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016.

### Background

CPSI, founded in 1979, is a leading provider of healthcare information technology ("IT") solutions and services for rural and community hospitals and post-acute care facilities. With our January 2016 acquisition of Healthland Holding Inc. ("HHI"), CPSI is now the parent of five companies - Evident, LLC ("Evident"), TruBridge, LLC ("TruBridge"), Healthland Inc. ("Healthland"), American HealthTech, Inc. ("AHT"), and Rycan Technologies, Inc. ("Rycan"). Our combined companies are focused on helping improve the health of the communities we serve, connecting communities for a better patient care experience, and improving the financial operations of our customers. The individual contributions of each of our five wholly-owned subsidiaries towards this combined focus are as follows: Evident, formed in April 2015, provides comprehensive electronic health record ("EHR") solutions and services for rural and community hospitals, including those solutions previously sold under the CPSI name as well as an expanded range of offerings targeted specifically at rural and community healthcare organizations.

TruBridge focuses exclusively on providing business management, consulting and managed IT services to rural and community healthcare organizations, regardless of their IT vendor.

Healthland, acquired in the acquisition of HHI, provides integrated technology solutions and services to small rural, community, and critical access hospitals.

AHT, acquired in the acquisition of HHI, is one of the nation's largest providers of financial and clinical technology solutions and services for post-acute care facilities.

Rycan, acquired in the acquisition of HHI, provides revenue cycle management workflow and automation software to rural and community hospitals, healthcare systems, and skilled nursing organizations.

The combined company currently supports approximately 1,300 acute care facilities and over 3,300 post-acute care facilities with a geographically diverse customer mix within the domestic rural and community healthcare market. Our customers primarily consist of rural and community hospitals with 300 or fewer acute care beds, with hospitals having 100 or fewer beds comprising approximately 95% of our hospital EHR customer base.

As discussed in this Item under "Results of Operations by Segment" below, we now manage our operations using three operating segments which are also our reportable segments: (1) acute care EHR, (2) post-acute care EHR and (3) TruBridge.

### Acute Care EHR

Our Acute Care EHR segment consists of acute care software solutions and support sales generated by Evident and Healthland.

### Post-acute Care EHR

Our Post-acute Care EHR segment consists of post-acute care software solutions and support sales generated by AHT.

### TruBridge

Our TruBridge segment primarily consists of business management, consulting and managed IT services sales generated by TruBridge and the sale of Rycan's revenue cycle management workflow and automation software.

### Management Overview

Historically we have primarily sought revenue growth through sales of healthcare IT systems and related services to existing and new customers within our target market, a strategy that has resulted in a ten-year compounded annual growth rate in legacy revenues (i.e., revenues related to our legacy Evident and TruBridge operations) of

approximately 4.5% as of the end of our most recently completed fiscal year. Important to our potential for continued long-term revenue growth is our ability to

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sell new and additional products and services to our existing customer base, including cross-selling opportunities presented with the acquisition of HHI. We believe that as our combined customer base grows, the demand for additional products and services, including business management, consulting and managed IT services, will also continue to grow, supporting further increases in recurring revenues. We also expect to drive revenue growth from new product development that we may generate from our research and development activities.

January 2016 marked an important milestone for CPSI, as we announced the completion of our acquisition of HHI, the first major acquisition in the Company's history. With this acquisition, CPSI now has a presence in well over 1,000 rural and community hospitals and over 3,300 post-acute care facilities, adding significantly to our already substantial recurring revenue base and further expanding our ability to generate organic recurring revenue growth through additional cross-selling opportunities now available within the combined company. We believe that the addition of HHI and its clients and products will enhance our ability to grow our business and compete in the markets that we serve.

Our business model is designed such that, as revenue growth materializes, earnings and profitability growth are naturally bolstered through increased future margin realization. Once a hospital has installed our solutions, we continue to provide support services to the customer on an ongoing basis and make available to the customer our broad portfolio of business management, consulting, and managed IT services. The provision of these services typically requires fewer resources than the initial system installation, resulting in increased overall gross margins. We also look to increase margins through cost containment measures where appropriate. For example, during 2016 we instituted several changes related to our employee benefits offerings, including a spousal carve-out for healthcare benefits. Additionally, during the first quarter of 2017 we instituted a one-time, voluntary severance program offering those employees meeting certain predetermined criteria severance packages involving continuing periodic cash payments and healthcare benefits for varying periods, depending upon the individual's years of service with the Company. Lastly, the acquisition of HHI in January of 2016 presents us with additional opportunities to leverage the greater operating efficiencies of the combined entity in order to drive further earnings and profitability growth in the future.

Turbulence in the U.S. and worldwide economies and financial markets impacts almost all industries. While the healthcare industry is not immune to economic cycles, we believe it is more significantly affected by U.S. regulatory and national health projects than by the economic cycles of our economy. Additionally, healthcare organizations with a large dependency on Medicare and Medicaid populations, such as rural and community hospitals, have been affected by the challenging financial condition of the federal government and many state governments and government programs. Accordingly, we recognize that prospective hospital customers often do not have the necessary capital to make investments in information technology. Additionally, in response to these challenges, hospitals have become more selective regarding where they invest capital, resulting in a focus on strategic spending that generates a return on their investment. Despite these challenges, we believe healthcare information technology is often viewed as more strategically beneficial to hospitals than other possible purchases because the technology offers the possibility of a quick return on investment. Information technology also plays an important role in healthcare by improving safety and efficiency and reducing costs. Additionally, we believe most hospitals recognize that they must invest in healthcare information technology to meet current and future regulatory, compliance and government reimbursement requirements.

In recent years, there have been significant changes to provider reimbursement by the U.S. federal government, followed by commercial payers and state governments. There is increasing pressure on healthcare organizations to reduce costs and increase quality, replacing fee-for-service in part by enrolling in an advanced payment model. This pressure could further encourage adoption of healthcare IT and increase demand for business management, consulting, and managed IT services as the future success of these healthcare providers is greatly dependent upon their ability to engage patient populations and to coordinate patient care across a multitude of settings, while optimizing operating efficiency along the way.

We have historically made financing arrangements available to customers on a case-by-case basis depending upon the various aspects of the proposed contract and customer attributes. These financing arrangements include other short-term payment plans and longer-term lease financing through us or third-party financing companies. For those

customers not seeking a financing arrangement, the payment schedule of the typical contract is structured to provide for a scheduling deposit due at contract signing, with the remainder of the contracted fees due at various stages of the installation process (delivery of hardware, installation of software and commencement of training, and satisfactory completion of a monthly accounting cycle or end-of-month operation by and as applicable for each respective application).

We have also historically made our software applications available to customers through "Software as a Service" or "SaaS" configurations, including our Cloud Electronic Health Record ("Cloud EHR") offering. These offerings are attractive to some customers because this configuration allows them to obtain access to advanced software products without a significant initial capital outlay. Although the broader enterprise software marketplace has been experiencing an increasing trend of SaaS



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arrangements in the past few years, this trend has been slower to develop within our market for new system installations and add-on sales to existing customers. However, we experienced a substantial increase in the prevalence of such arrangements within our system sales arrangements in 2015, a trend which continued in 2016 and we expect to continue for the foreseeable future. Unlike our historical perpetual license arrangements under which the related revenue is recognized effectively upon installation, the SaaS arrangements result in revenue being recognized monthly as the services are provided over the term of the arrangement. As a result, the effect of this trend on the Company's financial statements is reduced system sales revenues during the period of installation in exchange for increased recurring periodic revenues (reflected in system sales and support revenues) over the term of the SaaS arrangement.

American Recovery and Reinvestment Act of 2009

While ongoing financial challenges facing healthcare organizations have impacted and are expected to continue to impact the rural and community hospitals that comprise our target market, we believe that the financial incentives and penalties offered by the American Recovery and Reinvestment Act of 2009 (the "ARRA") for the adoption of qualifying EHRs have increased and will continue to support demand for healthcare information technology and will have a positive impact on our business prospects through at least 2018. As of June 30, 2017, incentive payments totaling over \$37 billion have been made to aid healthcare organizations in modernizing their operations through the acquisition and wide-spread use of healthcare information technology. Eligible hospitals could begin receiving these incentive payments in any year from 2011 through 2015, but the total incentive payment is decreased for hospitals that started receiving payments in 2014 and later. Additionally, reimbursements under Medicare have been reduced for those eligible healthcare providers that did not begin to demonstrate meaningful use of an EHR by October 1, 2014. The accelerated adoption of EHRs resulting from the ARRA's EHR incentive program has resulted in a narrowing market for new system installations and has accelerated the purchases of incremental applications by our existing customer base to satisfy the current meaningful use rules, thereby also narrowing the market for add-on sales to existing customers for meaningful use stage two-related incremental applications. Despite these narrowing markets, we expect to continue to benefit from the ARRA's EHR incentive program as the expanded requirements for continued eligibility for incentive payments and related payment adjustments for those healthcare providers not in compliance with meaningful use rules are expected to result in both an expanded replacement market for EHRs and additional orders from our existing customer base to purchase incremental applications necessary to satisfy such expanded requirements, particularly as the stage three meaningful use rules become effective. The stage three requirements are optional for 2017 and 2018, with all providers required to comply with the stage three requirements beginning in 2019. However, as the EHR replacement market is not likely to develop rapidly and revenues from add-on sales to existing customers for incremental stage three-related applications are not likely to significantly materialize until the related stage three rules become effective, our system sales revenues and profitability are expected to be materially and adversely affected during the short-term. Although we are pursuing other strategic initiatives designed to result in system sales revenue growth in the future in the form of selective expansion into English-speaking international markets, selective expansion within the 100 to 300 bed hospital market and targeted expansion for our ambulatory solutions, there can be no guarantee that such initiatives will prove successful or will benefit the Company in a sufficiently timely fashion to offset the short-term effects of the aforementioned narrowing markets. On August 2, 2017, the Centers for Medicare and Medicaid Services ("CMS") announced a final rule that effectively delays the requirement for stage three compliance from the first day of 2018 to the first day of 2019. The delay by the CMS is expected to delay some of the contract revenues we previously anticipated and there is a risk of further delays or reductions in the regulatory requirements imposed on hospitals, which could have an adverse effect on our revenues.

Health Care Reform

In March 2010, President Obama signed into law the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010, collectively referred to as the "Health Reform Laws." This sweeping legislation implemented changes to the healthcare and health insurance industries from 2010 through 2015, requiring substantially all U.S. citizens and legal residents to have qualifying health insurance coverage starting in 2014 and providing the means by which it will be made available to them. The Health Reform Laws have had little direct impact on our internal operation and do not appear to have had a significant impact on the businesses of our hospital

customers to date. However, we have not been able to determine at this point whether the ultimate impact will be positive, negative or neutral; it is likely that the Health Reform Laws will affect hospitals differently depending upon the populations they service. Rural and community hospitals typically service higher uninsured populations than larger urban hospitals and rely more heavily on Medicare and Medicaid for reimbursement. It remains to be seen whether the increase in the insured populations for rural and community hospitals, as well as the increase in Medicare and Medicaid reimbursements under the ARRA for hospitals that implement EHR technology, will be enough to offset cuts in Medicare and Medicaid reimbursements contained in the Health Reform Laws or as a result of sequestration or other federal legislation.

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We believe healthcare reform initiatives will continue during the foreseeable future. If adopted, some aspects of previously proposed reforms, such as further reductions in Medicare and Medicaid payments, could adversely affect the businesses of our customers and thereby harm our business.

## Results of Operations

Despite impressive growth in revenues from our TruBridge services, which management views as the primary agent for long-term revenue growth for CPSI, revenue challenges faced by our system sales and support operations have resulted in decreased total revenues as, during the six months ended June 30, 2017, we generated revenues of \$131.8 million from the sales of our products and services, compared to \$138.1 million during the six months ended June 30, 2016, a decrease of 4.6%. This decrease in revenues is primarily attributed to (1) the continuing challenging environment for add-on sales within our acute care EHR customer base, (2) the exhaustion of migration revenue opportunities for Healthland customers moving from the legacy Classic platform to Healthland's flagship Centriq platform, (3) the revenue impact of 2016-reported attrition within the Healthland customer base, and (4) decreased installation volumes of AHT's post-acute EHR solution. Despite the decrease in total revenues, our net income for the six months ended June 30, 2017 increased 450.4% due to the realization of acquisition-related synergies over the trailing twelve months and the lack of any significant transaction-related costs during the first six months of 2017. This improved profitability, coupled with more cash-advantageous changes in working capital, resulted in an improvement in cash flow from operations, increasing from cash used in operations of \$8.5 million during the first six months of 2016 to cash provided by operations of \$15.9 million during the first six months of 2017.

The following table sets forth certain items included in our results of operations for the three and six months ended June 30, 2017 and 2016, expressed as a percentage of our total revenues for these periods:

(In thousands)	Three Months Ended June 30,				Six Months Ended June 30,			
	2017		2016		2017		2016	
	Amount	% Sales	Amount	% Sales	Amount	% Sales	Amount	% Sales
<b>INCOME DATA:</b>								
Sales revenues:								
System sales and support	\$45,474	67.2 %	\$47,719	69.7 %	\$88,897	67.5 %	\$97,428	70.6 %
TruBridge	22,203	32.8 %	20,696	30.3 %	42,854	32.5 %	40,630	29.4 %
Total sales revenues	67,677	100.0 %	68,415	100.0 %	131,751	100.0 %	138,058	100.0 %
Costs of sales:								
System sales and support	18,859	27.9 %	21,886	32.0 %	37,789	28.7 %	44,153	32.0 %
TruBridge	11,933	17.6 %	11,616	17.0 %	23,520	17.9 %	22,903	16.6 %
Total costs of sales	30,792	45.5 %	33,502	49.0 %	61,309	46.5 %	67,056	48.6 %
Gross profit	36,885	54.5 %	34,913	51.0 %	70,442	53.5 %	71,002	51.4 %
Operating expenses:								
Product development	9,308	13.8 %	8,179	12.0 %	18,243	13.8 %	15,369	11.1 %
Sales and marketing	7,607	11.2 %	6,717	9.8 %	14,734	11.2 %	13,447	9.7 %
General and administrative	12,921	19.1 %	12,130	17.7 %	24,581	18.7 %	31,168	22.6 %
Amortization of acquisition-related intangibles	2,601	3.8 %	2,624	3.8 %	5,203	3.9 %	4,979	3.6 %
Total operating expenses	32,437	47.9 %	29,650	43.3 %	62,761	47.6 %	64,963	47.1 %
Operating income	4,448	6.6 %	5,263	7.7 %	7,681	5.8 %	6,039	4.4 %
Other income (expense):								
Other income	70	0.1 %	69	0.1 %	140	0.1 %	68	— %
Interest expense	(1,938 )	(2.9 )%	(1,642 )	(2.4 )%	(3,745 )	(2.8 )%	(3,110 )	(2.3 )%
Total other income (expense)	(1,868 )	(2.8 )%	(1,573 )	(2.3 )%	(3,605 )	(2.7 )%	(3,042 )	(2.2 )%
Income before taxes	2,580	3.8 %	3,690	5.4 %	4,076	3.1 %	2,997	2.2 %
Provision for income taxes	993	1.5 %	1,694	2.5 %	2,243	1.7 %	2,664	1.9 %
Net income	\$1,587	2.3 %	\$1,996	2.9 %	\$1,833	1.4 %	\$333	0.2 %



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Three Months Ended June 30, 2017 Compared with Three Months Ended June 30, 2016

Revenues. Total revenues for the three months ended June 30, 2017 decreased 1.1%, or \$0.7 million, compared to the three months ended June 30, 2016.

System sales and support revenues decreased by 4.7%, or \$2.2 million, from the three months ended June 30, 2016. System sales and support revenues were comprised of the following for the three months ended June 30, 2017 and 2016.

(In thousands)	Three Months Ended	
	June 30, 2017	June 30, 2016
Recurring system sales and support revenues <sup>(1)</sup>	\$33,109	\$34,236
Non-recurring system sales and support revenues <sup>(2)</sup>	12,365	13,483
Total system sales and support revenue	\$45,474	\$47,719

<sup>(1)</sup> Mostly comprised of support and maintenance, subscriptions, and SaaS revenues.

<sup>(2)</sup> Mostly comprised of installation revenues from the sale of our acute and post-acute EHR solutions and related applications under a perpetual (non-subscription) licensing model.

Nonrecurring system sales and support revenues decreased \$1.1 million, or 8.2%, primarily as Evident's add-on volumes decreased and the market for Healthland migrations from the legacy Classic platform to Healthland's flagship Centriq platform continues to decrease. Related to Evident's new system installation volumes, we completed installation of our Thrive EHR solution at ten new hospital clients during the three months ended June 30, 2017 (one of which was under a Cloud EHR arrangement, under which the related costs are all captured in the period of installation with the resulting revenue recognized ratably over the contractual term as the services are provided) compared to five during the three months ended June 30, 2016 (none of which were under a Cloud EHR arrangement), with a resulting revenue increase of \$2.8 million. Evident's add-on sales decreased by \$0.9 million due to lower installation volumes of Emergency Department Information Systems and Thrive Provider EHR. Platform migration opportunities for Healthland customers moving from Classic to Centriq are naturally decreasing over time as we have completed most migrations for this finite population, resulting in a \$1.7 million decrease in nonrecurring revenues from our Healthland operations as we completed three migrations during the three months ended June 30, 2016 compared to one in the three months ended June 30, 2017. These decreased installation revenues at Evident and Healthland have been compounded by decreased installations of AHT's post-acute EHR solution, resulting in a \$0.9 million decrease in related revenues.

Recurring system sales and support revenues decreased \$1.1 million, or 3.3%. Our recently acquired Healthland customer base contains a heavy concentration of calendar year-end support and maintenance renewal terms. As a result, the majority of the revenue impact related to Healthland attrition through 2016 customer support terminations did not materialize until the first quarter of 2017.

TruBridge revenues increased 7.3%, or \$1.5 million, from the three months ended June 30, 2016. Our hospital customers operate in an environment typified by rising costs and increased complexity and are increasingly seeking to alleviate themselves of the ever-increasing administrative burden of operating their own business office functions, resulting in an expanded customer base for our accounts receivable management services (increasing 5.2%, or \$0.3 million). Our insurance services revenues have increased 15.7%, or \$0.7 million, primarily as our recent acquisition of HHI exposes Rycan's solutions, which we consider to be best-of-breed, to a broader and more robust sales channel. Our IT managed services revenues have increased 19.5%, or \$0.4 million, as we continue to see increasing demand for remote hosting for our acute and post-acute EHR solutions. Our medical coding services have increased 31.4%, or \$0.3 million, as new key customers have been added. These increases have been partially offset by a 12.2%, or \$0.1 million, decrease in consulting revenues as ICD-10 related projects have decreased based on the related regulatory compliance deadline and decreased implementations of our Computerized Practitioner Order Entry ("CPOE") and

Physician Documentation applications have limited the related consulting opportunities.

Costs of Sales. Total costs of sales decreased by 8.1%, or \$2.7 million, from the second quarter of 2016. As a percentage of total revenues, costs of sales decreased from 49.0% in the second quarter of 2016 to 45.5% in the second quarter of 2017.

Costs of system sales and support decreased by 13.8%, or \$3.0 million, from the three months ended June 30, 2016 primarily due to decreased equipment costs and travel associated with the overall decrease in nonrecurring system sales revenues discussed above, leading to a combined \$1.6 million decrease. Payroll and related costs decreased by \$1.5 million, or 12.3%, primarily as the realization of HHI acquisition synergies over the trailing twelve months have resulted in a decrease in

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associated headcount. As a result, the gross margin on system sales and support increased to 58.5% in the three months ended June 30, 2017 from 54.1% in the three months ended June 30, 2016.

Our costs associated with TruBridge increased 2.7%, or \$0.3 million, in the three months ended June 30, 2017 with the largest contributing factor being an increase in payroll and related costs of 8.7%, or \$0.6 million, as a result of adding more employees during the trailing twelve months in order to support and develop our growing customer base and increase capacity in advance of anticipated future increases in demand. The gross margin on these services increased to 46.3% in the three months ended June 30, 2017 from 43.9% in the three months ended June 30, 2016. This margin improvement is the result of revenues materializing during the second quarter of 2017 for which the related investments in capacity had been made in prior periods.

**Product Development Costs.** Product development expense consists primarily of compensation and other employee-related costs (including stock-based compensation) and infrastructure costs incurred, but not capitalized, for new product development and product enhancements. Product development costs increased 13.8%, or \$1.1 million, from the three months ended June 30, 2016, as a result of increased headcount dedicated to functionality additions and enhancements across the product lines as well as integration across product lines.

**Sales and Marketing Expenses.** Sales and marketing expense increased 13.2%, or \$0.9 million, from the three months ended June 30, 2016, with the largest contributing factor being a \$0.6 million increase in commission expense resulting from the aforementioned increase in Evident's new system implementation volumes and related revenues and continued bookings growth for TruBridge. Adding to the increased commission expense was an approximately \$0.4 million increase in marketing program expenses due to more aggressive marketing of our family of community healthcare companies as we continue to mature our brand positioning after the HHI acquisition.

**General and Administrative Expenses.** General and administrative expenses increased 6.5%, or \$0.8 million, from the three months ended June 30, 2016, mostly due to \$1.7 million of expense associated with a one-time, voluntary severance program that, although initiated during the first quarter of 2017, concluded during the second quarter of 2017. Additionally, our three separate national user conferences held during the second and third quarters of 2016 were combined into a single national user conference across our entire customer base for 2017. This newly combined conference took place during the second quarter of 2017, resulting in an increase in related expenses of \$0.4 million. This combined \$2.1 million increase in severance and national user conference expenses were partially offset by a \$0.6 million decrease in legal and accounting primarily as a result of litigation-related insurance proceeds, a \$0.4 million decrease in HHI transaction costs, and a \$0.5 million decrease in payroll and related costs due to the realization of synergies during the trailing twelve months from the HHI acquisition.

**Amortization of Acquisition-Related Intangibles.** Amortization expense associated with acquisition-related intangible assets remained relatively unchanged from the second quarter of 2016.

As a percentage of total revenues, total operating expenses increased to 47.9% in the second quarter of 2017 compared to 43.3% in the second quarter of 2016.

**Total Other Income (Expense).** Total other income (expense) increased from expense of \$1.6 million during the three months ended June 30, 2016 to expense of \$1.9 million during the three months ended June 30, 2017, as market conditions have resulted in increased interest rates paid on our variable-rate debt obligations.

As a result of the foregoing factors, income before taxes decreased by 30.1%, or \$1.1 million, from the three months ended June 30, 2016.

**Income Taxes.** Our effective income tax rates for the three months ended June 30, 2017 and 2016 were 38.5% and 45.9%, respectively. During the three months ended June 30, 2016 the identification of nondeductible facilitative transaction costs and adjustments in our estimated state effective tax rate resulted in combined additional income tax expense of \$0.4 million, increasing the period's effective tax rate by 11.2%. Conversely, during the three months ended June 30, 2017 we experienced a shortfall tax expense related to restricted stock of \$0.2 million that increased the effective rate by 6.1% due to the adoption of ASU 2016-09.

**Net Income.** Net income for the three months ended June 30, 2017 decreased by \$0.4 million to a net income of \$1.6 million, or \$0.11 per basic and diluted share, compared with net income of \$2.0 million, or \$0.15 per basic and diluted share, for the three months ended June 30, 2016. Net income represented 2.3% of revenue for the three months ended June 30, 2017, compared to 2.9% of revenue for the three months ended June 30, 2016.





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Results of Operations by Segment. We operate in three reportable segments: (1) Acute Care EHR, (2) Post-acute Care EHR and (3) TruBridge. See Note 14 above for additional information on our segment reporting. The following table presents a summary of our operating segment information for the three months ended June 30, 2017 and 2016, respectively:

(In thousands)	Three Months Ended	
	June 30, 2017	June 30, 2016
Sales revenues:		
Acute Care EHR	\$39,394	\$40,754
Post-acute Care EHR	6,080	6,965
TruBridge	22,203	20,696
Total revenues	\$67,677	\$68,415
Costs of sales:		
Acute Care EHR	\$16,836	\$19,364
Post-acute Care EHR	2,023	2,522
TruBridge	11,933	11,616
Total costs of sales	\$30,792	\$33,502
Gross profit:		
Acute Care EHR	\$22,558	\$21,390
Post-acute Care EHR	4,057	4,443
TruBridge	10,270	9,080
Total gross profit	\$36,885	\$34,913

**Acute Care EHR**

Acute Care EHR revenues decreased \$1.4 million, or 3.3%, primarily as Evident's add-on volumes decreased and the market for Healthland migrations from the legacy Classic platform to Healthland's flagship Centriq platform continues to decrease. Related to Evident's new system installation volumes, we completed installation of our Thrive EHR solution at ten new hospital clients during the three months ended June 30, 2017 (one of which was under a Cloud EHR arrangement) compared to five during the three months ended June 30, 2016 (none of which were under a Cloud EHR arrangement), with a resulting revenue increase of \$2.8 million. Evident's add-on sales decreased by \$0.9 million due to lower installation volumes of Emergency Department Information Systems and Thrive Provider EHR. Platform migration opportunities for Healthland customers moving from Classic to Centriq are naturally decreasing over time as we have completed most migrations for this finite population, resulting in a \$1.7 million decrease in nonrecurring revenues from our Healthland operations as we completed three migrations during the three months ended June 30, 2016 compared to one in the three months ended June 30, 2017. Recurring Acute Care revenues decreased \$1.2 million, or 4.0%. Our recently acquired Healthland customer base contains a heavy concentration of calendar year-end support and maintenance renewal terms. As a result, the majority of the revenue impact related to Healthland attrition through 2016 customer support terminations did not materialize until the first quarter of 2017 and we continued to experience that impact in the second quarter.

Acute Care EHR costs of sales decreased by 13.1%, or \$2.5 million, from the second quarter of 2016, primarily due to decreased equipment costs and travel associated with the decrease in nonrecurring sales revenues discussed above, leading to a combined \$1.5 million decrease. Payroll and related costs decreased by \$1.0 million, or 9.0%, primarily as the realization of HHI acquisition synergies over the trailing twelve months have resulted in a decrease in associated headcount. As a result, the gross margin on Acute Care EHR revenues increased to 57.3% in the three months ended June 30, 2017 from 52.5% in the three months ended June 30, 2016.

Post-acute Care EHR

Post-acute Care EHR revenues decreased by 12.7%, or \$0.9 million, from the three months ended June 30, 2016, due to decreased AHT product line installations during the three months ended June 30, 2017.

Post-acute Care EHR costs of sales decreased by 19.8%, or \$0.5 million, from the three months ended June 30, 2016, primarily due to reduced associated headcount resulting from acquisition-related synergies captured during the trailing twelve months combined with the repurposing of certain individuals to our corporate-wide product development teams.

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The gross margin on Post-acute Care EHR revenues increased from 63.8% during the three months ended June 30, 2016 to 66.7% during the three months ended June 30, 2017 due to the aforementioned cost of sales reductions.

**TruBridge**

TruBridge revenues increased 7.3%, or \$1.5 million, from the three months ended June 30, 2016. Our hospital customers operate in an environment typified by rising costs and increased complexity and are increasingly seeking to alleviate themselves of the ever-increasing administrative burden of operating their own business office functions, resulting in an expanded customer base for our accounts receivable management services (increasing 5.2%, or \$0.3 million). Our insurance services revenues have increased 15.7%, or \$0.7 million, primarily as our recent acquisition of HHI exposes Rycaan's solutions, which we consider to be best-of-breed, to a broader and more robust sales channel. Our IT managed services revenues have increased 19.5%, or \$0.4 million, as we continue to see increasing demand for remote hosting for our acute and post-acute EHR solutions. Our medical coding services have increased 31.4%, or \$0.3 million, as new key customers have been added. These increases have been partially offset by a 12.2%, or \$0.1 million, decrease in consulting revenues as ICD-10 related projects have decreased based on the related regulatory compliance deadline and decreased implementations of our Computerized Practitioner Order Entry ("CPOE") and Physician Documentation applications have limited the related consulting opportunities.

Our costs associated with TruBridge increased 2.7%, or \$0.3 million, in the three months ended June 30, 2017 with the largest contributing factor being an increase in payroll and related costs of 8.7%, or \$0.6 million, as a result of adding more employees during the trailing twelve months in order to support and develop our growing customer base and increase capacity in advance of anticipated future increases in demand. The gross margin on these services increased to 46.3% in the three months ended June 30, 2017 from 43.9% in the three months ended June 30, 2016. This margin improvement is the result of revenues materializing during the second quarter of 2017 for which the related investments in capacity had been made in prior periods.

**Six Months Ended June 30, 2017 Compared with Six Months Ended June 30, 2016**

Revenues. Total revenues for the six months ended June 30, 2017 decreased 4.6%, or \$6.3 million, compared to the six months ended June 30, 2016.

System sales and support revenues decreased by 8.8%, or \$8.5 million, from the six months ended June 30, 2016. System sales and support revenues were comprised of the following for the six months ended June 30, 2017 and June 30, 2016:

(In thousands)	Six Months Ended	
	June 30, 2017	June 30, 2016
Recurring system sales and support revenues <sup>(1)</sup>	66,725	68,735
Non-recurring system sales and support revenues <sup>(2)</sup>	22,172	28,693
Total system sales and support revenue	\$88,897	\$97,428

<sup>(1)</sup> Mostly comprised of support and maintenance, subscriptions, and SaaS revenues.

<sup>(2)</sup> Mostly comprised of installation revenues from the sale of our acute and post-acute EHR solutions and related applications under a perpetual (non-subscription) licensing model.

Nonrecurring system sales and support revenues decreased \$6.5 million, or 22.7%, primarily as Evident's system add-on volumes decreased and the market for Healthland migrations from the legacy Classic platform to Healthland's flagship Centriq platform continues to decrease. Related to Evident's new system installation volumes, we completed installation of our Thrive EHR solution at thirteen new hospital clients during the six months ended June 30, 2017 (two of which were under a Cloud EHR arrangement) compared to eleven new hospital clients during the six months ended June 30, 2016 (one of which was under a Cloud EHR arrangement), with a resulting revenue increase of \$1.4 million. Evident's add-on sales decreased by \$2.6 million due to lower installation volumes of Emergency Department Information Systems and Thrive Provider EHR. Platform migration opportunities for Healthland customers moving

from Classic to Centriq are naturally decreasing over time as we have completed most migrations for this finite population, resulting in a \$3.0 million decrease in nonrecurring revenues from our Healthland operations as we completed six migrations during the six months ended June 30, 2016 compared to one in the six months ended June 30, 2017. These decreased installation revenues at Evident and Healthland have been compounded by decreased installations of AHT's post-acute EHR solution, resulting in a \$1.7 million decrease in related revenues.

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Recurring system sales and support revenues decreased \$2.0 million, or 2.9%. Our recently acquired Healthland customer base contains a heavy concentration of calendar year-end support and maintenance renewal terms. As a result, the majority of the revenue impact related to Healthland attrition through 2016 customer support terminations did not materialize until the first quarter of 2017.

TruBridge revenues increased 5.5%, or \$2.2 million, from the six months ended June 30, 2016. The current environment has resulted in an expanded customer base for our private pay services (increasing 3.3%, or \$0.2 million) and accounts receivable management services (increasing 5.0%, or \$0.6 million). Our insurance services revenues have increased 12.0%, or \$1.1 million, primarily as our recent acquisition of HHI exposes Ryca's solutions, which we consider to be best-of-breed, to a broader and more robust sales channel. Our IT managed services revenues have increased 18.5%, or \$0.8 million, as we continue to see increasing demand for remote hosting for our acute and post-acute EHR solutions. Our medical coding services have increased 16.9%, or \$0.3 million, as new key customers have been added. These increases have been partially offset by a 22.3%, or \$0.5 million, decrease in consulting revenues as ICD-10 related projects have decreased based on the related regulatory compliance deadline and decreased implementations of our Computerized Practitioner Order Entry ("CPOE") and Physician Documentation applications have limited the related consulting opportunities.

Costs of Sales. Total costs of sales decreased by 8.6%, or \$5.7 million, from the six months ended June 30, 2016. As a percentage of total revenues, costs of sales decreased from 48.6% in the six months ended June 30, 2016 to 46.5% in the six months ended June 30, 2017.

Costs of system sales and support decreased by 14.4%, or \$6.4 million, from the six months ended June 30, 2016 primarily due to decreased equipment costs and travel associated with the overall decrease in nonrecurring system sales revenues discussed above, leading to a combined \$3.2 million decrease. Payroll and related costs decreased by \$2.1 million, or 8.7%, primarily as the realization of HHI acquisition synergies over the trailing twelve months have resulted in a decrease in associated headcount. As a result, the gross margin on system sales and support increased to 57.5% in the six months ended June 30, 2017 from 54.7% in the six months ended June 30, 2016.

Our costs associated with TruBridge increased 2.7%, or \$0.6 million, with the largest contributing factor being an increase in payroll and related costs of 8.3%, or \$1.1 million, as a result of adding more employees during the trailing twelve months in order to support and develop our growing customer base and increase capacity in advance of anticipated future increases in demand. The gross margin on these services increased to 45.1% in the six months ended June 30, 2017 from 43.6% in the six months ended June 30, 2016. This margin improvement is the result of revenues materializing during the second quarter of 2017 for which the related investments in capacity had been made in prior periods.

Product Development Costs. Product development expense consists primarily of compensation and other employee-related costs (including stock-based compensation) and infrastructure costs incurred, but not capitalized, for new product development and product enhancements. Product development costs increased 18.7%, or \$2.9 million, from the six months ended June 30, 2016, as a result of increased headcount dedicated to functionality additions and enhancements across the product lines as well as integration across product lines.

Sales and Marketing Expenses. Sales and marketing expense increased 9.6%, or \$1.3 million, from the six months ended June 30, 2016, with the largest contributing factor being a \$0.9 million increase in commission expense resulting from the aforementioned increase in Evident's new system implementation volumes and related revenues and continued bookings growth for TruBridge. Adding to the increased commission expense was an approximately \$0.7 million increase in marketing program expenses due to more aggressive marketing of our family of community healthcare companies as we continue to mature our brand positioning after the HHI acquisition.

General and Administrative Expenses. General and administrative expenses decreased 21.1%, or \$6.6 million, from the six months ended June 30, 2016, primarily due to \$8.0 million in HHI transaction costs incurred during the six months ended June 30, 2016 with no such costs during the six months ended June 30, 2017. Adding to the decrease in HHI transaction costs is a \$0.7 million decrease in costs associated with the employer match portion of our defined contribution retirement plan resulting from changes to plan design to achieve better distribution of employer match throughout the year and a \$2.3 million decrease in payroll and related costs due to the realization of synergies during the trailing twelve months from the HHI acquisition. Partially offsetting this combined \$11.1 million decrease in HHI

transaction costs, employer match expenses, and payroll and related costs has been \$2.1 million of expense associated with a one-time, voluntary retirement program that was concluded during the first six months of 2017. Additionally, our three separate national user conferences held during the second and third quarters of 2016 were combined into a single national user conference across our entire customer base for 2017. This newly combined conference took place during the second quarter of 2017, resulting in an increase in related expenses of \$0.4 million.

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Amortization of Acquisition-Related Intangibles. Amortization expense associated with acquisition-related intangible assets increased by 4.5%, or \$0.2 million, from the six months ended June 30, 2016. This is due to seven additional days of amortization during the six months ended June 30, 2017 due to the closing date of the HHI acquisition.

As a percentage of total revenues, total operating expenses increased to 47.6% in the six months ended June 30, 2017 compared to 47.1% in the six months ended June 30, 2016.

Total Other Income (Expense). Total other income (expense) increased from expense of \$3.0 million during the six months ended June 30, 2016 to expense of \$3.6 million during the six months ended June 30, 2017, as market conditions have resulted in increased interest rates paid on our variable-rate debt obligations.

As a result of the foregoing factors, income before taxes increased by 36.0%, or \$1.1 million, from the six months ended June 30, 2016.

Income Taxes. Our effective income tax rates for the six months ended June 30, 2017 and 2016 were 55.0% and 88.9%, respectively. During the six months ended June 30, 2016 the identification of nondeductible facilitative transaction costs resulted in additional income tax expense of \$1.5 million, increasing the period's effective tax rate by 49.1%. Conversely, during the six months ended June 30, 2017 we experienced a shortfall tax expense related to restricted stock of \$0.9 million that increased the effective tax rate by 22.6% due to the adoption of ASU 2016-09.

Net Income. Net income for the six months ended June 30, 2017 increased by \$1.5 million to a net income of \$1.8 million, or \$0.13 per basic and diluted share, compared with net income of \$0.3 million, or \$0.03 per basic and diluted share, for the six months ended June 30, 2016. Net income represented 1.4% of revenue for the six months ended June 30, 2017, compared to 0.2% of revenue for the six months ended June 30, 2016.

Results of Operations by Segment. We operate in three reportable segments: (1) Acute Care EHR, (2) Post-acute Care EHR and (3) TruBridge. See Note 14 above for additional information on our segment reporting. The following table presents a summary of our operating segment information for the six months ended June 30, 2017 and 2016, respectively:

(In thousands)	Six Months Ended	
	June 30, 2017	June 30, 2016
Sales revenues:		
Acute Care EHR	\$76,525	\$83,494
Post-acute Care EHR	12,372	13,934
TruBridge	42,854	40,630
Total revenues	\$131,751	\$138,058
Costs of sales:		
Acute Care EHR	33,753	39,250
Post-acute Care EHR	4,036	4,903
TruBridge	23,520	22,903
Total costs of sales	\$61,309	\$67,056
Gross profit:		
Acute Care EHR	42,772	44,244
Post-acute Care EHR	8,336	9,031
TruBridge	19,334	17,727
Total gross profit	\$70,442	\$71,002

Table of Contents**Acute Care EHR**

Acute Care EHR revenues decreased \$7.0 million, or 8.3%, primarily as Evident's system add-on volumes decreased and the market for Healthland migrations from the legacy Classic platform to Healthland's flagship Centriq platform continues to decrease. Related to Evident's new system installation volumes, we completed installation of our Thrive EHR solution at thirteen new hospital clients during the six months ended June 30, 2017 (two of which were under a Cloud EHR arrangement) compared to eleven new hospital clients during the six months ended June 30, 2016 (one of which was under a Cloud EHR arrangement), with a resulting revenue increase of \$1.4 million. Evident's add-on sales decreased by \$2.6 million due to lower installation volumes of Emergency Department Information Systems and Thrive Provider EHR. Platform migration opportunities for Healthland customers moving from Classic to Centriq are naturally decreasing over time as we have completed most migrations for this finite population, resulting in a \$3.0 million decrease in nonrecurring revenues from our Healthland operations as we completed six migrations during the six months ended June 30, 2016 compared to one in the six months ended June 30, 2017. Recurring Acute Care revenues decreased \$2.1 million, or 3.6%. Our recently acquired Healthland customer base contains a heavy concentration of calendar year-end support and maintenance renewal terms. As a result, the majority of the revenue impact related to Healthland attrition through 2016 customer support terminations did not materialize until the first quarter of 2017.

Acute Care EHR costs of sales decreased by 14.0%, or \$5.5 million, from the six months ended June 30, 2016, primarily due to decreased equipment costs and travel associated with the decrease in nonrecurring sales revenues discussed above, leading to a combined \$2.8 million decrease. Payroll and related costs decreased by \$1.7 million, or 7.9%, primarily as the realization of HHI acquisition synergies over the trailing twelve months have resulted in a decrease in associated headcount. As a result, the gross margin on Acute Care EHR revenues increased to 55.9% in the six months ended June 30, 2017 from 53.0% in the six months ended June 30, 2016.

**Post-acute Care EHR**

Post-acute Care EHR revenues decreased by 11.2%, or \$1.6 million, from the six months ended June 30, 2016, due to decreased AHT product line installations during the six months ended June 30, 2017.

Post-acute Care EHR costs of sales decreased by 17.7%, or \$0.9 million, from the six months ended June 30, 2016, primarily due to a \$0.4 million decrease in equipment costs and travel expenses associated with the decreased system sales volumes discussed above, coupled with reduced associated headcount resulting from acquisition-related synergies captured during the trailing twelve months combined with the repurposing of certain individuals to our corporate-wide product development teams.

The gross margin on Post-acute Care EHR revenues increased from 64.8% during the six months ended June 30, 2016 to 67.4% during the six months ended June 30, 2017 due to the aforementioned cost of sales reductions.

**TruBridge**

TruBridge revenues increased 5.5%, or \$2.2 million, from the six months ended June 30, 2016. Our hospital customers operate in an environment typified by rising costs and increased complexity and are increasingly seeking to alleviate themselves of the ever increasing administrative burden of operating their own business office functions, resulting in an expanded customer base for our private pay services (increasing 3.3%, or \$0.2 million) and accounts receivable management services (increasing 5.0%, or \$0.6 million). Our insurance services revenues have increased 12.0%, or \$1.1 million, primarily as our recent acquisition of HHI exposes Rycan's solutions, which we consider to be best-of-breed, to a broader and more robust sales channel. Our IT managed services revenues have increased 18.5%, or \$0.8 million, as we continue to see increasing demand for remote hosting for our acute and post-acute EHR solutions. Our medical coding services have increased 16.9%, or \$0.3 million, as new key customers have been added. These increases have been partially offset by a 22.3%, or \$0.5 million decrease in consulting revenues as ICD-10 related projects have decreased based on the related regulatory compliance deadline and decreased implementations of our Computerized Practitioner Order Entry ("CPOE") and Physician Documentation applications have limited the related consulting opportunities.

Our costs associated with TruBridge increased 2.7%, or \$0.6 million, with the largest contributing factor being an increase in payroll and related costs of 8.3%, or \$1.1 million, as a result of adding more employees during the trailing twelve months in order to support and develop our growing customer base and increase capacity in advance of



anticipated future increases in demand. The gross margin on these services increased to 45.1% in the six months ended June 30, 2017 from 43.6% in the six months ended June 30, 2016. This margin improvement is the result of revenues materializing during the second quarter of 2017 for which the related investments in capacity had been made in prior periods.

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### Liquidity and Capital Resources

#### Sources of Liquidity

As of June 30, 2017, our principal sources of liquidity consisted of cash and cash equivalents of \$1.7 million and our remaining borrowing capacity under the Revolving Credit Facility (as defined below) compared to \$2.2 million of cash and cash equivalents as of December 31, 2016. As noted previously, in January 2016 we completed our acquisition of HHI. In conjunction with the acquisition, we entered into a syndicated credit agreement (the "Credit Agreement,") described further below, with Regions Bank ("Regions") serving as administrative agent, which provided for a \$125 million term loan facility (the "Term Loan Facility") and a \$50 million revolving credit facility (the "Revolving Credit Facility" and, together with the Term Loan Facility, the "Credit Facilities"). The cash portion of the purchase price for our acquisition of HHI was primarily funded by the \$125 million Term Loan Facility and \$25 million borrowed under the Revolving Credit Facility. As of June 30, 2017, we had \$145.3 million in principal amount of indebtedness outstanding under the Credit Facilities.

We believe that our cash and cash equivalents of \$1.7 million as of June 30, 2017, the future operating cash flows of the combined entity, and our remaining borrowing capacity under the Revolving Credit Facility of \$23.5 million as of June 30, 2017, taken together, provide adequate resources to fund ongoing cash requirements for the next twelve months. We cannot provide assurance that our actual cash requirements will not be greater than we expect as of the date of filing of this Form 10-Q. If sources of liquidity are not available or if we cannot generate sufficient cash flow from operations during the next twelve months, we may be required to obtain additional sources of funds through additional operational improvements, capital market transactions, asset sales or financing from third parties, a combination thereof or otherwise. We cannot provide assurance that these additional sources of funds will be available or, if available, would have reasonable terms.

#### Operating Cash Flow Activities

Net cash provided by operating activities increased \$24.4 million, from \$8.5 million used in operations for the six months ended 2016 to \$15.9 million provided by operations for the six months ended 2017. This increase is primarily due to the aforementioned \$1.5 million increase in net income and more cash-advantageous changes in working capital. During the first six months of 2016, we invested heavily in improving the working capital of the HHI entities post-acquisition in order to normalize the aging of vendor payables and improve acquired vendor relationships, resulting in a combined cash outflow of \$10.1 million during the first six months of 2016. Comparatively, the timing of vendor payments during the first six months of 2017 resulted in expansion of these liabilities and a resulting benefit to cash flows of \$6.8 million, for a total beneficial swing in cash flows from these working capital components of \$16.9 million.

Additionally, our acquisition of HHI in January 2016 included significant deferred revenue balances, the amortization of which benefited revenues during the first six months of 2016 with no corresponding cash benefit. Conversely, deferred revenue balances grew during the six months ended June 30, 2017 due to a high volume of advance billings for third party subscriptions, providing cash benefits with no related revenue impact. These deferred revenue dynamics alone resulted in an \$11.3 million improvement in cash flows as displayed in the condensed consolidated statement of cash flows.

These cash flow improvements have been partially offset by an increasing level of customer financing arrangements for the purchase of our EHR systems. The first six months of 2017 saw financing receivables expansion that was \$3.7 million more than such expansion during the first six months of 2016.

#### Investing Cash Flow Activities

Net cash used in investing activities decreased to \$0.5 million in the six months ended June 30, 2017 from \$151.8 million used during the six months ended June 30, 2016. We utilized cash (net of cash acquired) of \$162.6 million for the acquisition of HHI during the six months ended June 30, 2016, partially offset by sales of investments in available-for-sale securities of \$10.9 million during this period. We do not anticipate the need for significant capital expenditures during the remainder of 2017.

#### Financing Cash Flow Activities

During the six months ended June 30, 2017, our financing activities used net cash of \$15.9 million, as we paid \$9.8 million in long term debt principle and we declared and paid dividends in the amount of \$6.1 million. Financing cash

flow activities provided \$139.1 million during the six months ended June 30, 2016, primarily due to the proceeds of the aforementioned credit facility of \$156.6 million partially offset by \$17.2 million cash paid in dividends.

We believe that paying dividends is an effective way of providing an investment return to our stockholders and a beneficial use of our cash. However, the declaration of dividends by CPSI is subject to compliance with the terms of our Credit Agreement and the discretion of our Board of Directors which may decide to change or terminate the Company's dividend

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policy at any time. Our Board of Directors will continue to take into account such matters as general business conditions, capital needs, our financial results and such other factors as our Board of Directors may deem relevant.

**Credit Agreement**  
 As noted above, in conjunction with our acquisition of HHI in January 2016, we entered into a Credit Agreement which provided for a \$125 million Term Loan Facility and a \$50 million Revolving Credit Facility. As of June 30, 2017, we had \$118.8 million in principal amount outstanding under the Term Loan Facility and \$26.5 million in principal amount outstanding under the Revolving Credit Facility.

The Term Loan Facility bears interest at a rate per annum equal to an applicable margin plus, at our option, either (1) the Adjusted LIBOR rate for the relevant interest period, (2) an alternate base rate determined by reference to the greater of (a) the prime lending rate of Regions, (b) the federal funds rate for the relevant interest period plus one half of one percent per annum and (c) the one month LIBOR rate plus one percent per annum, or (3) a combination of (1) and (2). The applicable margin will range from 2.25% to 3.50% for LIBOR loans and 1.25% to 2.50% for base rate loans, in each case based on our consolidated leverage ratio (as defined in the Credit Agreement). Interest on the outstanding principal of the Term Loan Facility will be payable on the last day of each month, in the case of each base rate loan, and on the last day of each interest period (but no less frequently than every three months), in the case of LIBOR loans. Principal payments are due on the last day of each fiscal quarter beginning March 31, 2016, with quarterly principal payments of approximately \$0.8 million in 2016, approximately \$1.6 million in 2017, approximately \$2.3 million in 2018, approximately \$3.1 million in 2019 and approximately \$3.9 million in 2020, with the remainder due at maturity on January 8, 2021 or such earlier date as the obligations under the Credit Agreement become due and payable pursuant to the terms of the Credit Agreement (the “Maturity Date”).

Borrowings under the Revolving Credit Facility bear interest at a rate per annum equal to an applicable margin plus, at our option, either (1) the Adjusted LIBOR rate for the relevant interest period or (2) an alternate base rate determined by reference to the greatest of (a) the prime lending rate of Regions, (b) the federal funds rate for the relevant interest period plus one half of one percent per annum and (c) the one month LIBOR rate plus one percent per annum. The applicable margin will range from 2.25% to 3.50% for LIBOR loans and 1.25% to 2.50% for base rate loans, in each case based on our consolidated leverage ratio. Interest on borrowings under the Revolving Credit Facility is payable on the last day of each month, in the case of each base rate loan, and on the last day of each interest period (but no less frequently than every three months), in the case of LIBOR loans. The Revolving Credit Facility includes a \$5 million swingline sublimit, with swingline loans bearing interest at the alternate base rate plus the applicable margin. Any principal outstanding under the Revolving Credit Facility is due and payable on the Maturity Date.

The Term Loan Facility and amounts borrowed under the Revolving Credit Facility are secured pursuant to a Pledge and Security Agreement, dated January 8, 2016, among the parties identified as obligors therein and Regions, as collateral agent (the “Security Agreement”), on a first priority basis by a security interest in substantially all of the tangible and intangible assets (subject to certain exceptions) of the Company and certain subsidiaries of the Company, as guarantors (collectively, the “Subsidiary Guarantors”), including certain registered intellectual property and the capital stock of certain of the Company’s direct and indirect subsidiaries. Our obligations under the Credit Agreement are also guaranteed by the Subsidiary Guarantors.

The Credit Agreement provides incremental facility capacity of \$50 million, subject to certain conditions. The Credit Agreement includes a number of restrictive covenants that, among other things and in each case subject to certain exceptions and baskets, impose operating and financial restrictions on the Company and the Subsidiary Guarantors, including the ability to incur additional debt; incur liens and encumbrances; make certain restricted payments, including paying dividends on the Company's equity securities or payments to redeem, repurchase or retire the Company's equity securities (which are subject to our compliance, on a pro forma basis to give effect to the restricted payment, with the fixed charge coverage ratio and consolidated leverage ratio described below); enter into certain restrictive agreements; make investments, loans and acquisitions; merge or consolidate with any other person; dispose of assets; enter into sale and leaseback transactions; engage in transactions with affiliates; and materially alter the business we conduct. In addition, the Company is required to comply with a minimum fixed charge coverage ratio of 1.25:1.0 throughout the duration of the Credit Agreement and a maximum consolidated leverage ratio (as defined in the Credit Agreement, as amended) of 3.50:1.0 through September 30, 2017, 3.00:1.0 from October 1, 2017 through

September 30, 2018, and 2.50:1.0 thereafter. The Credit Agreement also contains customary representations and warranties, affirmative covenants and events of default. We believe that we were in compliance with the covenants contained in the Credit Agreement as of June 30, 2017.

The Credit Agreement requires the Company to mandatorily prepay the Term Loan Facility and amounts borrowed under the Revolving Credit Facility with (i) 100% of net cash proceeds from certain sales and dispositions, subject to certain reinvestment rights, (ii) 100% of net cash proceeds from certain issuances or incurrences of additional debt, (iii) 50% of net cash proceeds from certain issuances or sales of equity securities, subject to a step down to 0% if the Company's consolidated

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leverage ratio is no greater than 2.50:1.0, and (iv) beginning with the fiscal year ending December 31, 2016, 50% of excess cash flow (minus certain specified other payments), subject to a step down to 0% of excess cash flow if the Company's consolidated leverage ratio is no greater than 2.50:1.0. The Company is permitted to voluntarily prepay the Term Loan Facility and amounts borrowed under the Revolving Credit Facility at any time without penalty, subject to customary "breakage" costs with respect to prepayments of LIBOR rate loans made on a day other than the last day of any applicable interest period.

### Backlog

Backlog consists of revenues we reasonably expect to recognize over the next 12 months under existing contracts. The revenues to be recognized may relate to a combination of one-time fees for system sales and recurring fees for support and maintenance and TruBridge services. As of June 30, 2017, we had a total backlog of approximately \$37.2 million in connection with non-recurring system purchases and approximately \$217.2 million in connection with recurring payments under support and maintenance, Cloud EHR contracts, and TruBridge services. Of the \$37.2 million in non-recurring backlog as of June 30, 2017, approximately \$16.1 million represents firm orders for incremental applications associated with stage three meaningful use requirements of the ARRA's EHR incentive program. On August 2, 2017, the CMS announced a final rule that effectively delays the requirement for stage three compliance from the first day of 2018 to the first day of 2019. As a result, we are unable to estimate with a reasonable amount of certainty what amount of the stage three backlog is expected to be recognized as revenue over the next twelve months. As of June 30, 2016, we had a twelve-month backlog of approximately \$15.5 million in connection with non-recurring system purchases and approximately \$210.8 million in connection with recurring payments under support and maintenance and TruBridge services.

### Off-Balance Sheet Arrangements

We had no off-balance sheet arrangements, as defined by Item 303(a)(4) of SEC Regulation S-K, as of June 30, 2017. The Company has other lease rights and obligations that it accounts for as operating leases that may be reclassified as balance sheet arrangements under accounting pronouncements recently finalized by the FASB.

### Critical Accounting Policies and Estimates

Our Management Discussion and Analysis is based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make subjective or complex judgments that may affect the reported financial condition and results of operations. We base our estimates on historical experience and other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the reported values of assets, liabilities, revenues, expenses and other financial amounts that are not readily apparent from other sources. Actual results may differ from these estimates and these estimates may differ under different assumptions or conditions. We continually evaluate the information used to make these estimates as our business and the economic environment changes.

In our Annual Report on Form 10-K for the year ended December 31, 2016, we identified our critical accounting policies related to revenue recognition, allowance for doubtful accounts, allowance for credit losses, and estimates. There have been no significant changes to these critical accounting policies during the six months ended June 30, 2017.

### Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Our exposure to market risk relates primarily to the potential change in the British Bankers Association London Interbank Offered Rate ("LIBOR"). We had \$145.3 million of outstanding borrowings under our Credit Facilities with Regions Bank at June 30, 2017. The Term Loan Facility and Revolving Credit Facility bear interest at a rate per annum equal to an applicable margin plus (1) the Adjusted LIBOR rate for the relevant interest period, (2) an alternate base rate determined by reference to the greatest of (a) the prime lending rate of Regions, (b) the federal funds rate for the relevant interest period plus one half of one percent per annum and (c) the one month LIBOR rate plus one percent per annum, or (3) a combination of (1) and (2). Accordingly, we are exposed to fluctuations in interest rates on borrowings under the Credit Facilities. A one hundred basis point change in interest rate on our borrowings outstanding as of June 30, 2017 would result in a change in interest expense of approximately \$1.5 million annually. We did not have investments and do not utilize derivative financial instruments to manage our interest rate risks.



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Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to provide reasonable assurance that the information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the rules and forms promulgated by the Securities and Exchange Commission, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Because of the inherent limitations to the effectiveness of any system of disclosure controls and procedures, no evaluation of disclosure controls and procedures can provide absolute assurance that all control issues and instances of fraud, if any, with a company have been prevented or detected on a timely basis. Even disclosure controls and procedures determined to be effective can only provide reasonable assurance that their objectives are achieved.

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) pursuant to Rule 13a-15 of the Exchange Act. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

As previously disclosed under "Item 9A - Controls and Procedures" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016, the Company identified a material weakness related to the Company's business combination process. The Company identified deficiencies in its internal controls over review of third-party valuations and properly establishing and accounting for opening balance sheet amounts. The Company has taken actions to remediate the material weakness related to our internal control over financial reporting. We have made improvements to the design of the related controls, including standardized review procedures over third-party valuations. We intend to supplement our in-house accounting and financial reporting functions with third-party consultants with extensive experience in accounting for complex business combinations. However, as the Company did not complete another acquisition, neither we nor our external auditors tested the operating effectiveness of these newly designed controls.

Successful remediation of the material weakness described above requires review and evidence of the effectiveness of the related internal control processes as part of our periodic assessments of our internal control over financial reporting. As we continue to evaluate and work to enhance our internal control over financial reporting, we may determine that additional measures should be taken to address the material weakness described above or other control deficiencies, or that we should modify the remediation plan.

Except as noted in the preceding paragraphs, there were no changes in the Company's internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) during the quarter ended June 30, 2017 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.



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PART II  
OTHER INFORMATION

Item 1. Legal Proceedings.

From time to time, we are involved in routine litigation that arises in the ordinary course of business. We are not currently involved in any claims outside the ordinary course of business that are material to our financial condition or results of operations.

Item 1A. Risk Factors.

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem immaterial also may materially adversely affect our business, financial condition or operating results.

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

Not Applicable.

Item 3. Defaults Upon Senior Securities.

Not applicable.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

As previously reported, at the 2017 Annual Meeting of Stockholders (the "Annual Meeting") held on May 11, 2017, the Company's stockholders approved the 2014 Plan to increase the number of shares of common stock available for grant under the 2014 Plan from 700,000 to 2,100,000 shares. A more detailed summary of the principal features of the 2014 Plan can be found in the Company's definitive proxy statement for the Annual Meeting, as filed with the Securities and Exchange Commission on March 31, 2017 (the "Proxy"). The foregoing description does not purport to be complete and is qualified in its entirety by reference to such summary and the full text of the 2014 Plan filed as Appendix A to the Proxy and incorporated herein by reference.

Item 6. Exhibits.

- 3.1 Certificate of Incorporation (filed as Exhibit 3.4 to CPSI's Registration Statement on Form S-1 (Registration No. 333-84726) and incorporated herein by reference)
- 3.2 Amended and Restated Bylaws (filed as Exhibit 3 to CPSI's Current Report on Form 8-K dated October 28, 2013 and incorporated herein by reference)
- 10.1 Computer Programs and Systems, Inc. Amended and Restated 2014 Incentive Plan (filed as Appendix A to CPSI's Schedule 14A dated March 31, 2017 and incorporated herein by reference)
- 31.1 Certification of the Chief Executive Officer pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of the Chief Financial Officer pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certifications of the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101 Interactive Data Files for CPSI's Form 10-Q for the period ended June 30, 2017

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

COMPUTER PROGRAMS AND  
SYSTEMS, INC.

Date: August 8, 2017 By: /s/ J. Boyd Douglas  
J. Boyd Douglas  
President and Chief Executive Officer

Date: August 8, 2017 By: /S/ Matt J. Chambless  
Matt J. Chambless  
Chief Financial Officer

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