

Emdeon Inc.
Form 10-Q
November 12, 2009

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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 September 30, 2009
Commission file number 001-34435
EMDEON INC.
(Exact Name of Registrant as Specified in its Charter)**

<p style="text-align: center;">Delaware (State or Other Jurisdiction of Incorporation or Organization)</p> <p style="text-align: center;">3055 Lebanon Pike, Suite 1000 Nashville, TN (Address of Principal Executive Offices)</p>	<p>20-5799664 (I.R.S. Employer Identification No.)</p> <p>37214 (Zip Code)</p> <p>(615) 932-3000 (Registrant's Telephone Number, Including Area Code)</p>
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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. (Check one):

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input checked="" type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>
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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding as of November 11, 2009
Class A common stock, \$0.00001 par value	90,238,103
Class B common stock, \$0.00001 par value	24,752,955

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

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Emdeon Inc.
Condensed Consolidated Balance Sheets
(unaudited and amounts in thousands, except share and per share amounts)

	December 31, 2008	September 30, 2009
Assets		
Current assets:		
Cash and cash equivalents	\$ 71,478	\$ 194,989
Accounts receivable, net of allowance for doubtful accounts of \$4,576 and \$4,499 at December 31, 2008 and September 30, 2009, respectively	144,149	152,460
Deferred income tax assets	2,285	6,233
Prepaid expenses and other current assets	21,137	17,272
Total current assets	239,049	370,954
Property and equipment, net	136,038	144,324
Goodwill	646,851	703,008
Intangible assets, net	971,001	963,010
Other assets, net	7,340	1,526
Total assets	\$ 2,000,279	\$ 2,182,822
Liabilities and equity		
Current liabilities:		
Accounts payable	\$ 805	\$ 5,623
Accrued expenses	79,513	77,808
Deferred revenues	12,056	12,795
Current portion of long-term debt	17,244	5,139
Total current liabilities	109,618	101,365
Long-term debt, excluding current portion	807,986	796,768
Deferred income tax liabilities	159,811	151,869
Tax receivable agreement obligation to related parties		141,745
Other long-term liabilities	44,711	29,334
Commitments and contingencies		
Equity:		
Preferred stock (par value, \$0.00001), 25,000,000 shares authorized and 0 shares issued and outstanding		
Class A common stock (par value, \$0.00001), 400,000,000 shares authorized and 77,413,610 and 90,238,893 shares outstanding at December 31, 2008 and September 30, 2009, respectively	1	1
Class B exchangeable common stock (par value, \$0.00001), 52,000,000 shares authorized and 22,586,390 and 24,752,955 shares outstanding at December 31, 2008 and September 30, 2009, respectively		
Additional paid-in capital	670,702	732,836
Accumulated other comprehensive loss	(23,195)	(15,511)
Retained earnings	24,123	30,563

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Emdeon Inc. stockholders' equity	671,631	747,889
Noncontrolling interest	206,522	213,852
Total equity	878,153	961,741
Total liabilities and equity	\$ 2,000,279	\$ 2,182,822

See accompanying notes to the unaudited condensed consolidated financial statements.

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Emdeon Inc.
Condensed Consolidated Statements of Operations
(unaudited and amounts in thousands, except share and per share amounts)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2009	2008	2009
Revenue	\$ 212,808	\$ 235,462	\$ 635,666	\$ 679,888
Costs and expenses:				
Cost of operations (exclusive of depreciation and amortization below)	134,451	146,471	405,423	418,079
Development and engineering	7,312	10,045	21,029	24,425
Sales, marketing, general and administrative	22,220	33,823	69,309	85,146
Depreciation and amortization	25,710	26,667	71,979	77,051
Loss on abandonment of leased properties		482		742
Operating income	23,115	17,974	67,926	74,445
Interest income	(328)	(27)	(931)	(81)
Interest expense	20,410	17,219	49,899	52,330
Income before income tax provision	3,033	782	18,958	22,196
Income tax provision	3,512	9,245	11,202	12,885
Net income (loss)	(479)	(8,463)	7,756	9,311
Net income (loss) attributable to noncontrolling interest	766	(1,246)	2,620	2,871
Net income (loss) attributable to Emdeon Inc.	\$ (1,245)	\$ (7,217)	\$ 5,136	\$ 6,440
Net income (loss) per share Class A common stock:				
Basic	\$ (0.02)	\$ (0.09)	\$ 0.07	\$ 0.08
Diluted	\$ (0.02)	\$ (0.09)	\$ 0.07	\$ 0.08
Weighted average common shares outstanding:				
Basic	77,413,610	84,522,085	73,889,095	79,809,140
Diluted	77,413,610	84,522,085	73,889,095	79,856,588

See accompanying notes to the unaudited condensed consolidated financial statements.

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Emdeon Inc.									
Condensed Consolidated Statements of Equity									
(unaudited and amounts in thousands, except share and per share amounts)									
	Class A		Class B		Additional	Retained	Other	Non-	Total
	Common Stock		Common Stock		Paid-in	Earnings	Comprehensive	Controlling	Equity
	Shares	Amount	Shares	Amount	Capital	Earnings	(Loss)	Interest	Equity
Balance at January 1, 2008	52,000,000	\$ 1	48,000,000	\$	\$ 300,550	\$ 14,892	\$(14,474)	\$	\$ 300,969
Capital contribution from affiliates of General Atlantic LLC and Hellman & Friedman LLC for the purchase of HLTH Corporation's 48% interest in EBS Master LLC on February 8, 2008	25,413,610				578,409				578,409
Establish non-controlling interest on February 8, 2008			22,586,390		(210,585)		5,435	205,150	
Eliminate HLTH Corporation's 48% noncontrolling interest on February 8, 2008			(48,000,000)		1,345				1,345
Capital contribution from stockholders					1,300				1,300
Distribution to stockholders					(317)				(317)
Comprehensive income:									

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Net income					5,136		2,620	7,756	
Change in the fair value of interest rate swap, net of taxes						(9,594)		(9,594)	
Foreign currency translation adjustment						(3)		(3)	
Other comprehensive income amortization, net of taxes						4,743	1,383	6,126	
Total comprehensive income								4,285	
Balance at September 30, 2008	77,413,610	\$1	22,586,390	\$	\$ 670,702	\$20,028	\$(13,893)	\$209,153	\$ 885,991
Balance at January 1, 2009	77,413,610	\$1	22,586,390	\$	\$ 670,702	\$24,123	\$(23,195)	\$206,522	\$ 878,153
Capital contribution from stockholders					203			203	
Distribution to stockholders					(434)			(434)	
Reclassification of liability awards to equity awards					20,548		6,183	26,731	
Equity based compensation expense					3,022		832	3,854	
Purchase of eRx Network L.L.C.			1,850,000		3,530		318	19,707	23,555
Issuance of units of EBS Master to members of management, net of taxes			2,537,325		(11,979)		394	18,245	6,660
Issuance of Class A common stock	349,166				559		(18)	(851)	(310)

to employees and directors, net of taxes						
Conversion of EBS Master units held by eRx to shares of Class A common stock, net of taxes	1,850,000	(1,850,000)	21,919	(376)	(17,443)	4,100
Issuance of Class A shares in connection with initial public offering (includes costs paid in 2008)	10,725,000		145,211			145,211
Issuance of units of EBS Master to Emdeon Inc., net of taxes			13,799	(448)	(21,025)	(7,674)
Repurchase of Class A shares (to satisfy tax withholding obligation)	(101,515)		(1,573)			(1,573)
Repurchase of units of EBS Master issued to members of management, net of taxes		(370,760)	(1,115)	(74)	(3,500)	(4,689)
Tax receivable agreement with related parties, net of taxes			(131,556)			(131,556)
Issuance of Class A common stock upon vesting of Restricted Stock Units	2,632					
Comprehensive income:						
Net income			6,440		2,871	9,311
Changes in the fair value of interest rate swap, net of taxes				3,806	1,112	4,918

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Emdeon Inc.
Consolidated Statements of Cash Flows
(unaudited and amounts in thousands)

	For the Nine Months Ended September 30,	
	2008	2009
Operating activities		
Net income	\$ 7,756	\$ 9,311
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	71,979	77,051
Equity compensation expense	5,813	21,499
Deferred income tax expense (benefit)	4,925	(1,360)
Amortization of debt issuance costs	141	143
Amortization of debt discount	7,066	8,699
Amortization of discontinued cash flow hedge from other comprehensive income	7,011	5,968
Change in fair value of interest rate swap	(12,714)	
Loss on abandonment of leased properties		742
Loss on disposal of fixed assets	72	56
Changes in operating assets and liabilities:		
Accounts receivable	(16,968)	(3,990)
Prepaid expenses and other	(9,760)	4,911
Accounts payable	(3,392)	3,515
Accrued expenses and other liabilities	(2,507)	(6,199)
Deferred revenues	2,879	737
Net cash provided by operating activities	62,301	121,083
Investing activities		
Purchases of property and equipment	(13,942)	(30,563)
Payments for acquisitions, net of cash acquired	(19,090)	(75,871)
Purchase of EBS Master LLC	(306,260)	
Net cash used in investing activities	(339,292)	(106,434)
Financing activities		
Proceeds from initial public offering		148,261
Repurchase of Class A common stock		(1,573)
Repurchase of Units of EBS Master LLC		(5,372)
Debt principal payments	(5,662)	(21,663)
Payments on revolver		(10,201)
Payment of loan costs		(359)
Capital contributions from stockholders	307,451	203
Distribution to shareholders	(317)	(434)
Net cash provided by financing activities	301,472	108,862
Net increase in cash and cash equivalents	24,481	123,511
Cash and cash equivalents at beginning of period	33,687	71,478

Cash and cash equivalents at end of period	\$ 58,168	\$ 194,989
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See accompanying notes to the unaudited condensed consolidated financial statements.

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Emdeon Inc. (the Company) is a leading provider of revenue and payment cycle management solutions, connecting payers, providers and patients of the U.S. healthcare system. The Company's product and service offerings integrate and automate key business and administrative functions for healthcare payers and healthcare providers throughout the patient encounter, including pre-care patient eligibility and benefits verification, claims management and adjudication, payment integrity, payment distribution, payment posting and denial management and patient billing and payment collection.

Organization

Prior to November 2006, the group of companies that comprised Emdeon Business Services (EBS) was owned by HLTH Corporation (HLTH). EBS Master LLC (EBS Master) was formed by HLTH to act as a holding company for EBS. EBS Master, through its 100% owned subsidiary, Emdeon Business Services LLC (EBS LLC), owns EBS.

In September 2006, EBS Acquisition LLC (EBS Acquisition) was formed as a Delaware limited liability company by affiliates of General Atlantic LLC (General Atlantic). On November 16, 2006, pursuant to the terms of an Amended and Restated Agreement and Plan of Merger, dated as of November 15, 2006, among HLTH and certain of its subsidiaries (including EBS Master) and EBS Acquisition and two of its subsidiaries, a subsidiary of EBS Acquisition merged into a subsidiary of HLTH. As a result of the merger, EBS Acquisition acquired a 52% interest in EBS Master, and HLTH received approximately \$1,200,000 in cash and retained a 48% interest in EBS Master. The transactions through which EBS Acquisition acquired a 52% interest in EBS Master are referred to herein as the 2006 Transaction. The 2006 Transaction was financed with \$925,000 in bank debt and an equity investment of approximately \$320,000 by EBS Acquisition. As the 2006 Transaction was deemed to be a highly leveraged transaction, the 2006 Transaction was accounted for in accordance with Emerging Issues Task Force (EITF) Issue No. 88-16, *Basis in Leveraged Buyout Transactions*, and 52% of the net assets of EBS Master were stepped up to fair market value.

On February 8, 2008, HLTH sold its 48% noncontrolling interest in EBS Master to affiliates of General Atlantic and Hellman & Friedman LLC (H&F) for \$575,000 in cash (the 2008 Transaction). As a result, following the 2008 Transaction, EBS Master was owned 65.77% by affiliates of General Atlantic (including EBS Acquisition) and 34.23% by affiliates of H&F. See Note 4 for further information related to the 2008 Transaction.

In September 2008, EBS Acquisition was converted into a Delaware corporation, and the Company's name was changed to Emdeon Inc.

Reorganization

On August 5, 2009, the Company completed a restructuring (collectively, the reorganization transactions) in anticipation of completing an initial public offering.

Prior to the reorganization transactions, the Company owned a 52% interest in EBS Master and affiliates of General Atlantic and H&F owned the remaining 48% interest in EBS Master. The Company did not engage in any business or other activities except in connection with its investment in EBS Master and the reorganization transactions and had nominal assets other than its interest in EBS Master. In the reorganization transactions, the Company became the sole managing member of EBS Master and acquired additional interests in EBS Master.

Prior to the reorganization transactions, the Company was authorized to issue a single class of common stock. In connection with the reorganization transactions, the Company amended and restated its certificate of incorporation and is currently authorized to issue two classes of common stock: Class A common stock and Class B common stock.

Table of Contents**Emdeon Inc.****Notes to Condensed Consolidated Financial Statements
(unaudited and amounts in thousands, except share and per share amounts)**

As part of the reorganization transactions:

The Company amended and restated its certificate of incorporation and reclassified its outstanding common stock into an aggregate of 56,000,000 shares of its Class A common stock;

The Company redeemed 4,000,000 shares of Class A common stock from its existing stockholders in exchange for the rights by its existing stockholders to receive payments under a tax receivable agreement;

Another member of EBS Master, EBS Acquisition II, LLC (EBS Acquisition II), an affiliate of General Atlantic, was merged with a newly-formed subsidiary of the Company with the newly formed subsidiary being the surviving entity in the merger; EBS Acquisition II's members, all of whom are investment funds organized and controlled by General Atlantic, received an aggregate of 13,773,913 shares of the Company's Class A common stock, and the Company acquired, indirectly, an additional 13.52% interest in EBS Master;

One of the members of EBS Master, H&F Harrington AIV I, L.P. (H&F Harrington), an entity whose partners consist of investment funds organized and controlled by H&F, dissolved and distributed 1.06% of its interests in EBS Master to Hellman & Friedman Investors VI, L.P., its general partner (H&F GP), and 98.94% to H&F Harrington, Inc.; H&F Harrington, Inc. then merged with a newly-formed subsidiary of the Company with the newly formed subsidiary being the surviving entity in the merger; H&F Harrington, Inc.'s sole shareholder, H&F Harrington AIV II, L.P. (H&F AIV), an investment fund organized and controlled by H&F, received an aggregate of 11,639,697 shares of the Company's Class A common stock, and the Company acquired, indirectly, an additional 11.43% interest in EBS Master; and

Affiliates of H&F (or their successors) (the H&F Continuing LLC Members) continue to hold an aggregate of 22,586,390 units in EBS Master (EBS Units) (or 22.18% of the outstanding EBS Units) and were issued an aggregate of 22,586,390 shares of the Company's Class B common stock.

The Company accounted for the reorganization transactions using a carryover basis as the reorganization transactions are identical ownership exchanges among entities under common control. This is consistent with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Business Combinations Topic. The economic interests that the affiliates of General Atlantic and H&F held in EBS Master before the reorganization transactions did not change as a result of the reorganization transactions.

The reorganization was accounted for similar to a transaction between entities under common control. As EBS Acquisition II, H&F Harrington, and the H&F Continuing LLC Members did not purchase their interests in EBS Master until the 2008 Transaction, this reorganization did not materially impact the Company's financial statements through December 31, 2007. The financial statements for the three month and nine month periods ended September 30, 2008 and 2009, respectively are presented as if the H&F Continuing LLC Members represented the noncontrolling interest for the periods subsequent to February 9, 2008.

This reorganization and the changes to the capital structure are reflected in all periods presented.

Effective August 11, 2009, the Company priced its initial public offering of Class A common stock (the IPO) as more fully described in Note 10 to the unaudited condensed consolidated financial statements.

2. Basis of Presentation and Summary of Significant New Accounting Policies***Principles of Consolidation***

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and, in the opinion of management, reflect all normal recurring adjustments necessary for a fair presentation of results

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Emdeon Inc.

**Notes to Condensed Consolidated Financial Statements
(unaudited and amounts in thousands, except share and per share amounts)**

for the unaudited interim periods presented. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. The results of operations for the interim period are not necessarily indicative of the results to be obtained for the full fiscal year. All material intercompany accounts and transactions have been eliminated in the unaudited condensed consolidated financial statements.

Reclassifications

Certain reclassifications have been made to the prior period financial statements to conform to the current period presentation.

Recent Accounting Pronouncements

On January 1, 2009, the Company adopted the FASB ASC Business Combinations Topic. This topic expands the definition of a business and a business combination and generally requires the acquiring entity to recognize all of the assets and liabilities of the acquired business, regardless of the percentage ownership acquired, at their fair values. This topic also requires that contingent consideration and certain acquired contingencies be recorded at fair value on the acquisition date and that acquisition costs generally be expensed as incurred. The Company recorded approximately \$391 of acquisition related expenses in the nine months ended September 30, 2009 that, absent the adoption of this topic, would have been capitalized. These costs are included in the accompanying unaudited condensed consolidated statement of operations within sales, marketing, general and administrative expenses. As a result, net income for the nine months ended September 30, 2009 was reduced by approximately \$232 (\$0.00 per diluted Class A share).

On January 1, 2009, the Company adopted the provisions of the FASB ASC Fair Value Measurements and Disclosures Topic that relate to nonfinancial assets and liabilities that are not required or permitted to be measured at fair value on a recurring basis. Examples of such circumstances include fair value measurements associated with the initial recognition of assets and liabilities in a business combination and measurements of impairment following a goodwill impairment test or an impairment of a long-lived asset other than goodwill. The adoption of this topic had no material impact on the Company's unaudited condensed consolidated financial statements for the nine months ended September 30, 2009.

On January 1, 2009, the Company adopted the FASB ASC Consolidation Topic as it relates to noncontrolling interests in consolidated financial statements. The topic clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. Additionally, the topic changes the way the consolidated income statement is presented by requiring consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. The presentation and disclosure r