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 December 31, 2014

or

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

Commission file number: 001-12537

QUALITY SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

California	**95-2888568**
(State or other jurisdiction of incorporation or organization)	*(IRS Employer Identification No.)*
18111 Von Karman Avenue, Suite 700, Irvine, California	**92612**
(Address of principal executive offices)	*(Zip Code)*

(949) 255-2600
(Registrant's telephone number, including area code)

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 o

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 o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or 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 o
Non-accelerated filer o *(Do not check if a smaller reporting company)*	Small reporting company o

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

The number of outstanding shares of the Registrant's common stock as of January 20, 2015 was 60,285,615 shares.

QUALITY SYSTEMS, INC.

TABLE OF CONTENTS
FORM 10-Q
FOR THE THREE MONTHS ENDED DECEMBER 31, 2014

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

QUALITY SYSTEMS, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)
(Unaudited)

	December 31, 2014	March 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 113,640	$ 103,145
Restricted cash and cash equivalents	2,330	4,351
Marketable securities	11,182	10,656
Accounts receivable, net	105,879	110,181
Inventories	665	834
Income taxes receivable	3,391	8,366
Deferred income taxes, net	11,751	11,690
Other current assets	12,160	11,135
Total current assets	260,998	260,358
Equipment and improvements, net	21,636	22,801
Capitalized software costs, net	38,497	39,152
Intangibles, net	27,645	33,016
Goodwill	72,804	72,804
Other assets	17,671	16,927
Total assets	$ 439,251	$ 445,058
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 6,962	$ 7,888
Deferred revenue	67,756	71,077
Accrued compensation and related benefits	19,588	15,953
Dividends payable	10,697	10,686
Other current liabilities	33,906	18,282
Total current liabilities	138,909	123,886
Deferred revenue, net of current	1,611	2,187
Deferred compensation	5,477	4,809
Other noncurrent liabilities	10,753	19,086
Total liabilities	156,750	149,968
Commitments and contingencies (Note 11)		
Shareholders' equity:		
Common stock $0.01 par value; authorized 100,000 shares; issued and outstanding 60,285 and 60,206 shares at December 31, 2014 and March 31, 2014, respectively	603	602
Additional paid-in capital	197,727	194,739
Accumulated other comprehensive loss	(265)	(182)
Retained earnings	84,436	99,931
Total shareholders' equity	282,501	295,090
Total liabilities and shareholders' equity	$ 439,251	$ 445,058

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

QUALITY SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands, except per share data)
(Unaudited)

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
Revenues:				
Software and hardware	$ 16,339	$ 14,114	$ 45,312	$ 45,648
Implementation and training services	3,658	5,046	16,964	19,430
System sales	19,997	19,160	62,276	65,078
Maintenance	43,045	39,763	125,985	118,684
Electronic data interchange services	19,051	16,637	56,276	49,874
Revenue cycle management and related services	20,392	16,178	54,517	47,660
Other services	20,939	17,116	62,783	48,168
Maintenance, EDI, RCM and other services	103,427	89,694	299,561	264,386
Total revenues	123,424	108,854	361,837	329,464
Cost of revenue:				
Software and hardware	6,127	27,398	19,289	37,111
Implementation and training services	4,584	7,466	18,423	21,572
Total cost of system sales	10,711	34,864	37,712	58,683
Maintenance	7,365	5,642	21,064	16,206
Electronic data interchange services	11,956	10,276	35,970	31,722
Revenue cycle management and related services	14,246	11,736	40,154	34,144
Other services	10,082	8,537	32,423	26,054
Total cost of maintenance, EDI, RCM and other services	43,649	36,191	129,611	108,126
Total cost of revenue	54,360	71,055	167,323	166,809
Gross profit	69,064	37,799	194,514	162,655
Operating expenses:				
Selling, general and administrative	41,482	36,864	116,893	110,538
Research and development costs	18,468	13,175	51,602	26,404
Amortization of acquired intangible assets	904	1,219	2,795	3,673
Impairment of goodwill and other assets	—	5,873	—	5,873
Total operating expenses	60,854	57,131	171,290	146,488
Income (loss) from operations	8,210	(19,332)	23,224	16,167
Interest income (expense), net	(82)	121	41	(53)
Other income (expense), net	—	18	(17)	(391)
Income (loss) before income taxes	8,128	(19,193)	23,248	15,723
Provision for (benefit of) income taxes	1,452	(6,606)	6,659	5,244
Net income (loss)	$ 6,676	$ (12,587)	$ 16,589	$ 10,479
Other comprehensive income (loss):				
Foreign currency translation (net of $0 tax)	(101)	21	(177)	(172)
Unrealized gain (loss) on marketable securities (net of $0 tax)	68	(51)	94	(51)
Comprehensive income (loss)	$ 6,643	$ (12,617)	$ 16,506	$ 10,256
Net income (loss) per share:				
Basic	$ 0.11	$ (0.21)	$ 0.28	$ 0.18
Diluted	$ 0.11	$ (0.21)	$ 0.27	$ 0.17
Weighted-average shares outstanding:				
Basic	60,272	60,173	60,250	59,823
Diluted	60,855	60,173	60,813	59,984
Dividends declared per common share	$ 0.175	$ 0.175	$ 0.525	$ 0.525

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

QUALITY SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Nine Months Ended December 31,	
	2014	2013
Cash flows from operating activities:		
Net income	$ 16,589	$ 10,479
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	6,755	5,897
Amortization of capitalized software costs	10,190	9,353
Amortization of other intangibles	5,371	6,340
Loss on disposal of equipment and improvements	12	—
Provision for bad debts	38	2,791
Provision for inventory obsolescence	71	—
Share-based compensation	2,627	1,832
Deferred income taxes	(20)	896
Excess tax benefit from share-based compensation	—	(62)
Change in fair value of contingent consideration	1,533	(384)
Impairment of goodwill and other assets	—	25,971
Changes in assets and liabilities, net of amounts acquired:		
Accounts receivable	8,779	23,451
Inventories	98	(174)
Income taxes receivable	4,975	(15,270)
Other current assets	(221)	3,579
Other assets	(785)	(1,444)
Accounts payable	(1,084)	(6,842)
Deferred revenue	(3,897)	2,585
Accrued compensation and related benefits	3,635	1,777
Income taxes payable	(107)	(701)
Other current liabilities	4,152	454
Deferred compensation	668	748
Other noncurrent liabilities	(673)	295
Net cash provided by operating activities	58,706	71,571
Cash flows from investing activities:		
Additions to capitalized software costs	(9,535)	(18,914)
Additions to equipment and improvements	(5,444)	(7,448)
Proceeds from sales and maturities of marketable securities	10,352	12,990
Purchases of marketable securities	(10,995)	(14,091)
Purchase of Mirth	—	(35,033)
Net cash used in investing activities	(15,622)	(62,496)
Cash flows from financing activities:		
Excess tax benefit from share-based compensation	—	62
Proceeds from issuance of shares under employee plans	170	2,200
Dividends paid	(32,073)	(31,515)
Payment of contingent consideration related to acquisitions	(686)	(3,720)
Net cash used in financing activities	(32,589)	(32,973)
Net increase (decrease) in cash and cash equivalents	10,495	(23,898)
Cash and cash equivalents at beginning of period	103,145	105,999
Cash and cash equivalents at end of period	$ 113,640	$ 82,101

QUALITY SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS – (Continued)
(In thousands)
(Unaudited)

	Nine Months Ended December 31, 2014	Nine Months Ended December 31, 2013
Supplemental disclosures of cash flow information:		
Cash paid during the period for income taxes, net of refunds	$ 1,523	$ 20,443
Non-cash investing and financing activities:		
Effective September 9, 2013, the Company acquired Mirth in a transaction summarized as follows:		
Fair value of assets acquired		$ 62,771
Cash paid		(35,033)
Common stock issued at fair value		(7,882)
Fair value of contingent consideration		(13,307)
Liabilities assumed		$ 6,549

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

QUALITY SYSTEMS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except shares and per share data)
(Unaudited)

1. Summary of Significant Accounting Policies

Principles of Consolidation. The consolidated financial statements include the accounts of Quality Systems, Inc. and its wholly-owned subsidiaries, which consist of NextGen Healthcare Information Systems, LLC (“NextGen”), NextGen RCM Services, LLC, ViaTrack Systems, LLC (“ViaTrack”), Matrix Management Solutions, LLC, QSI Management, LLC, Quality Systems India Healthcare Private Limited (“QSIH”) and Mirth LLC and Mirth Limited (“Mirth”) (collectively, the “Company”). All intercompany accounts and transactions have been eliminated.

Basis of Presentation. The accompanying unaudited consolidated financial statements as of December 31, 2014 and for the three and nine months ended December 31, 2014 and 2013 have been prepared in accordance with the requirements of Quarterly Report on Form 10-Q and Article 10 of the Securities and Exchange Commission Regulation S-X and therefore do not include all information and notes which would be presented were such consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). These consolidated financial statements should be read in conjunction with the audited consolidated financial statements presented in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2014. Amounts related to disclosures of March 31, 2014 balances within these interim consolidated financial statements were derived from the aforementioned Annual Report on Form 10-K. In the opinion of management, the accompanying consolidated financial statements reflect all adjustments which are necessary for a fair presentation of the results of operations and cash flows for the periods presented. The results of operations for such interim periods are not necessarily indicative of results of operations to be expected for the full year.

References to amounts in the consolidated financial statement sections are in thousands, except shares and per share data, unless otherwise specified.

Revision. The accompanying consolidated statement of cash flows for the nine months ended December 31, 2013 has been retrospectively revised to reflect proceeds from sales and maturities of marketable securities and purchases of marketable securities as investing activities rather than operating activities, which resulted in a $1.1 million increase in cash provided by operating activities for the nine months ended December 31, 2013 and a corresponding increase in cash used in investing activities. The Company has evaluated the impact of the revision and determined that it did not have a material impact on any of its prior period annual and interim consolidated financial statements.

Significant Accounting Policies. There have been no material changes to the significant accounting policies from those disclosed in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

Share-Based Compensation. The following table shows total share-based compensation expense included in the consolidated statements of comprehensive income for the three and nine months ended December 31, 2014 and 2013:

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
Costs and expenses:				
Cost of revenue	$ 105	$ 90	$ 283	$ 253
Research and development costs	113	100	293	231
Selling, general and administrative	752	517	2,051	1,348
Total share-based compensation	970	707	2,627	1,832

The total income tax benefit related to share-based compensation was $0.3 million and $0.2 million for the three months ended December 31, 2014 and 2013, respectively. For the nine months ended December 31, 2014 and 2013, total income tax benefit related to share-based compensation was $0.8 million and $0.6 million, respectively.

Recent Accounting Standards. New accounting pronouncements implemented by the Company during the current year or requiring implementation in future periods are discussed below or in the notes, where applicable.

In May 2014, the FASB, along with the International Accounting Standards Board, issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers ("ASU 2014-09")*, which supersedes the revenue recognition requirements in ASC 605, *Revenue Recognition*. ASU 2014-09 provides enhancements to the quality and consistency of how revenue is reported while also improving comparability in the financial statements of companies reporting using International Financial Reporting Standards and GAAP. The core principle of this updated guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard also requires additional disclosure about revenue and provides improved guidance for multiple element arrangements. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Companies are permitted to adopt this new guidance following either a full retrospective or modified retrospective approach. Early adoption is not permitted. ASU 2014-09 is effective for the Company in the first quarter of fiscal 2018. The Company is currently evaluating the potential impact of implementation of this updated authoritative guidance on its consolidated financial statements.

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, *Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern ("ASU 2014-15")*, which incorporates and expands upon certain principles that currently exist in U.S. auditing standards. ASU 2014-15 provides guidance regarding management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. The new standard requires management to perform interim and annual evaluations and sets forth principles for considering the mitigating effect of management's plans. The standard mandates certain disclosures when conditions give rise to substantial doubt about a company’s ability to continue as a going concern within one year from the financial statement issuance date. ASU 2014-15 is effective for annual reporting periods ending after December 15, 2016, and all annual and interim periods thereafter. Early adoption is permitted. ASU 2014-15 is effective for the Company for fiscal year ending March 31, 2017. The Company does not expect the adoption of this new standard to have a material impact on its consolidated financial statements.

2. Fair Value Measurements

The following tables set forth by level within the fair value hierarchy the Company’s financial assets and liabilities that were accounted for at fair value on a recurring basis at December 31, 2014 and March 31, 2014:

	Balance at December 31, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
ASSETS				
Cash and cash equivalents (1)	$ 113,640	$ 113,640	$ —	$ —
Restricted cash and cash equivalents	2,330	2,330	—	—
Marketable securities (2)	11,182	11,182	—	—
	$ 127,152	$ 127,152	$ —	$ —
LIABILITIES				

Contingent consideration related to acquisitions	$ 15,760	$ —	$ —	$ 15,760
	$ 15,760	$ —	$ —	$ 15,760

	Balance at March 31, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
ASSETS				
Cash and cash equivalents (1)	$ 103,145	$ 103,145	$ —	$ —
Restricted cash and cash equivalents	4,351	4,351	—	—
Marketable securities (2)	10,656	10,656	—	—
	$ 118,152	$ 118,152	$ —	$ —
LIABILITIES				
Contingent consideration related to acquisitions	$ 14,913	$ —	$ —	$ 14,913
	$ 14,913	$ —	$ —	$ 14,913

(1) Cash equivalents consists of money market funds.
(2) Marketable securities consist of fixed-income securities, including certificates of deposit, corporate bonds and notes, and municipal securities.

The Company’s contingent consideration liability is accounted for at fair value on a recurring basis and is adjusted to fair value when the carrying value differs from fair value. The fair value adjustments are reflected as a component of selling, general and administrative expense. Key assumptions include discount rates and probability-adjusted achievement of strategic targets that are not observable in the market. The categorization of the framework used to measure fair value of the contingent consideration liability is considered Level 3 due to the subjective nature of the unobservable inputs used. The fair values of the contingent consideration liability were estimated based on the probability of achieving certain business milestones.

The following table presents activity in the Company’s financial assets and liabilities measured at fair value using significant unobservable inputs (Level 3), as of and for the nine months ended December 31, 2014:

		Total Liabilities
Balance as of April 1, 2014	$	14,913
Earnout payments		(686)
Fair value adjustments		1,533
Balance as of December 31, 2014	$	15,760

Non-Recurring Fair Value Measurements

The Company has certain assets, including goodwill and other intangible assets, which are measured at fair value on a non-recurring basis and are adjusted to fair value only if an impairment charge is recognized. The categorization of the framework used to measure fair value of the assets is considered Level 3 due to the subjective nature of the unobservable inputs used. During the nine months ended December 31, 2014, there were no adjustments to fair value of such assets.

3. Goodwill

The Company tests goodwill for impairment annually during its first fiscal quarter, referred to as the annual test date. The Company will also test for impairment between annual test dates if an event occurs or circumstances change that would indicate the carrying amount may be impaired. During the three months ended December 31, 2014, the Company has not identified any events or circumstances that would require an interim goodwill impairment test.

The Company does not amortize goodwill as it has been determined to have an indefinite useful life.

Goodwill by reporting unit consists of the following:

		March 31, 2014		December 31, 2014
QSI Dental Division (1)	$	7,289	$	7,289
NextGen Division		33,225		33,225
RCM Services Division		32,290		32,290
Total goodwill	$	72,804	$	72,804

(1) QSI Dental Division goodwill is presented on a basis consistent with that of the management reporting structures within QSI. For the purposes of testing goodwill for impairment annually and as otherwise may be required, however, the QSI Dental Division goodwill is allocated to all business units that derive cash flows from the products associated with the acquired goodwill. For all periods presented in this report, the allocation resulted in substantially all of such goodwill being ascribed to the NextGen Division.

4. Intangible Assets

The Company's definite-lived intangible assets, other than capitalized software development costs, are summarized as follows:

	December 31, 2014							
		Customer Relationships		Trade Name & Contracts		Software Technology		Total
Gross carrying amount	$	22,050	$	3,368	$	23,510	$	48,928
Accumulated amortization		(14,224)		(2,023)		(5,036)		(21,283)
Net intangible assets	$	7,826	$	1,345	$	18,474	$	27,645

	March 31, 2014							
		Customer Relationships		Trade Name & Contracts		Software Technology		Total
Gross carrying amount	$	22,050	$	3,368	$	23,510	$	48,928
Accumulated amortization		(11,837)		(1,599)		(2,476)		(15,912)
Net intangible assets	$	10,213	$	1,769	$	21,034	$	33,016

Amortization expense related to customer relationships and trade name & contracts that is included as operating expenses in the consolidated statements of comprehensive income was $905 and $1,209 for the three months ended December 31, 2014 and 2013, respectively. Amortization expense related to software technology that is included in cost of revenue for software and hardware was $858 and $1,069 for the three months ended December 31, 2014 and 2013, respectively.

Amortization expense related to customer relationships and trade name & contracts that is included as operating expenses in the consolidated statements of comprehensive income was $2,811 and $3,541 for the nine months ended December 31, 2014 and 2013, respectively. Amortization expense related to software technology that is included in cost of revenue for software and hardware was $2,560 and $2,799 for the nine months ended December 31, 2014 and 2013, respectively.

The following table represents the remaining estimated amortization of definite-lived intangible assets as of December 31, 2014:

For the year ended March 31,		
2015 (remaining three months)	$	1,756
2016		7,024
2017		6,553
2018		4,301
2019		3,517
2020 and beyond		4,494
Total	$	27,645

5. Capitalized Software Costs

The Company's capitalized software costs are summarized as follows:

	December 31, 2014		March 31, 2014	
Gross carrying amount	$	109,990	$	100,455
Accumulated amortization		(71,493)		(61,303)
Net capitalized software costs	$	38,497	$	39,152

Amortization expense related to capitalized software costs was $3,073 and $4,050 for the three months ended December 31, 2014 and 2013, respectively.

Amortization expense related to capitalized software costs was $10,190 and $9,353 for the nine months ended December 31, 2014 and 2013, respectively.

The following table presents the remaining estimated amortization of capitalized software costs as of December 31, 2014. The estimated amortization is comprised of (i) amortization of released products and (ii) the expected amortization for products that are not yet available for sale based on their estimated economic lives and projected general release dates.

For the year ended March 31,		
2015 (remaining three months)	$	3,000
2016		13,800
2017		9,500
2018		4,200
2019		4,000
2020 and beyond		3,997
Total	$	38,497

6. Composition of Certain Financial Statement Captions

Accounts receivable include amounts related to maintenance and services that were billed but not yet rendered at each period end. Undelivered maintenance and services are included as a component of the deferred revenue balance on the accompanying consolidated balance sheets.

	December 31, 2014	March 31, 2014
Accounts receivable, gross	$ 119,705	$ 127,006
Sales return reserve	(9,282)	(10,530)
Allowance for doubtful accounts	(4,544)	(6,295)
Accounts receivable, net	$ 105,879	$ 110,181

Inventories are summarized as follows:

	December 31, 2014	March 31, 2014
Computer systems and components	$ 665	$ 834

Equipment and improvements are summarized as follows:

	December 31, 2014	March 31, 2014
Computer equipment	$ 41,892	$ 37,322
Furniture and fixtures	10,308	9,395
Leasehold improvements	8,918	8,874
	61,118	55,591
Accumulated depreciation and amortization	(39,482)	(32,790)
Equipment and improvements, net	$ 21,636	$ 22,801

Current and non-current deferred revenue are summarized as follows:

	December 31, 2014	March 31, 2014
Maintenance	$ 14,954	$ 15,482
Implementation services	31,729	36,634
Annual license services	10,252	11,176
Undelivered software and other (1)	10,821	7,785
Deferred revenue	$ 67,756	$ 71,077
Deferred revenue, net of current	$ 1,611	$ 2,187

(1) Includes deferred revenue for Software as a Service ("SaaS") and other subscriptions.

Accrued compensation and related benefits are summarized as follows:

	December 31, 2014	March 31, 2014
Payroll, bonus and commission	$ 9,548	$ 6,193
Vacation	10,040	9,760
Accrued compensation and related benefits	$ 19,588	$ 15,953

Other current and non-current liabilities are summarized as follows:

	December 31, 2014	March 31, 2014
Contingent consideration and other liabilities related to acquisitions	$ 8,904	$ 1,052
Customer deposits	4,564	76
Accrued consulting	2,858	1,707
Care services liabilities	2,260	4,351
Accrued EDI expense	2,097	1,702
Professional services	1,893	170
Accrued royalties	1,641	1,418
Deferred rent	1,211	964
Self insurance reserve	797	2,090
Other accrued expenses	7,681	4,752
Other current liabilities	$ 33,906	$ 18,282
Contingent consideration and other liabilities related to acquisitions	$ 7,399	$ 14,736
Deferred rent	2,634	3,509
Income tax payable	720	841
Other non-current liabilities	$ 10,753	$ 19,086

7. Income Taxes

The provision for (benefit of) income taxes for the three months ended December 31, 2014 and 2013 was approximately $1.5 million and $(6.6) million, respectively. The effective tax rates were 17.9% and 34.4% for the three months ended December 31, 2014 and 2013, respectively. The effective rate for the three months ended December 31, 2014 decreased as compared to the same prior year period primarily due to favorable discrete items included in the current period related to the enactment of the federal research and development tax credit statute, which had expired on December 31, 2013 and on December 19, 2014 was retroactively extended through December 31, 2014. The non-deductible portion of the Hospital impairment charge in the prior year also resulted in an incremental decrease in the effective tax rate for the three months ended December 31, 2014.

The provision for income taxes for the nine months ended December 31, 2014 and 2013 was approximately $6.7 million and $5.2 million, respectively. The effective tax rates were 28.6% and 33.4% for the nine months ended December 31, 2014 and 2013, respectively. The effective rate for the nine months ended December 31, 2014 decreased as compared to the same prior year period primarily due to an increase in benefit from the federal research and development tax credit partially offset by a decrease in benefit from the qualified production activities deduction. The non-deductible portion of the Hospital impairment charge in the prior year also resulted in an incremental decrease in the effective tax rate for the nine months ended December 31, 2014.

The deferred tax assets and liabilities have been shown net in the accompanying consolidated balance sheets based on the long-term or short-term nature of the items that give rise to the deferred amount. The Company expects to receive the full benefit of the deferred tax assets recorded with the exception of a specific state tax credit for which the Company has recorded a valuation allowance.

Uncertain tax positions As of December 31, 2014, the Company had recorded a liability of $777 for unrecognized tax benefits related to various federal, state and local income tax matters. If recognized, this amount would reduce the Company’s effective tax rate. The tax liability for the nine months ended December 31, 2014 decreased from the same prior year period by $423 due to changes in reserves for state and local income tax liabilities, expiring statute of limitations, and certain tax positions related to acquired companies.

The Company is no longer subject to U.S. federal income tax examinations for tax years before 2013. With few exceptions, the Company is no longer subject to state income tax examinations for tax years before 2010. The Company does not anticipate that total unrecognized tax benefits will significantly change due to the settlement of audits or the expiration of statute of limitations within the next twelve months.

8. Earnings per Share

The Company provides presentation of “basic” and “diluted” earnings per share (“EPS”). Shares discussed below are in thousands.

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
Net income (loss)	$ 6,676	$ (12,587)	$ 16,589	$ 10,479
Basic net income (loss) per share:				
Weighted-average shares outstanding — Basic	60,272	60,173	60,250	59,823
Basic net income (loss) per common share	$ 0.11	$ (0.21)	$ 0.28	$ 0.18
Net income (loss)	$ 6,676	$ (12,587)	$ 16,589	$ 10,479
Diluted net income (loss) per share:				
Weighted-average shares outstanding — Basic	60,272	60,173	60,250	59,823
Effect of potentially dilutive securities	583	—	563	161
Weighted-average shares outstanding — Diluted	60,855	60,173	60,813	59,984
Diluted net income (loss) per common share	$ 0.11	$ (0.21)	$ 0.27	$ 0.17

The computation of diluted net income per share does not include 1,731 and 1,653 options to acquire shares of common stock for the three and nine months ended December 31, 2014, respectively, because their inclusion would have an anti-dilutive effect on net income per share.

The computation of diluted net income per share does not include 1,386 and 1,347 options to acquire shares of common stock for the three and nine months ended December 31, 2013, respectively, because their inclusion would have an anti-dilutive effect on net income (loss) per share.

9. Share-Based Awards

Employee Stock Option and Incentive Plans

In October 2005, the Company's shareholders approved a stock option and incentive plan (the "2005 Plan") under which 4,800,000 shares of common stock were reserved for the issuance of awards, including incentive stock options and non-qualified stock options, stock appreciation rights, restricted stock, unrestricted stock, restricted stock units, performance shares, performance units (including performance options) and other share-based awards. The 2005 Plan provides that employees and directors of the Company may, at the discretion of the Board of Directors or a duly designated compensation committee, be granted certain share-based awards. In the case of option awards granted under the 2005 Plan, the exercise price of each option is determined based on the date of grant and expire no later than 10 years from the date of grant. Awards granted pursuant to the 2005 Plan are subject to the vesting schedule or performance metrics set forth in the agreements pursuant to which they are granted. Upon a change of control of the Company, as such term is defined in the 2005 Plan, awards under the 2005 Plan will fully vest under certain circumstances. The 2005 Plan expires on May 25, 2015, unless terminated earlier by the Board of Directors. As of December 31, 2014, there were 1,711,676 outstanding options, 78,872 outstanding shares of restricted stock, restricted stock units and performance based restricted stock, and 2,222,988 shares available for future grant under the 2005 Plan.

A summary of stock option transactions during the nine months ended December 31, 2014 follows:

	Number of Shares	Weighted-Average Exercise Price per Share	Weighted-Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (in thousands)
Outstanding, April 1, 2014	1,370,101	$ 27.85	5.8	
Granted	459,650	15.97	7.4	
Forfeited/Canceled	(118,075)	25.47	4.5	
Outstanding, December 31, 2014	1,711,676	$ 24.83	5.7	$ —
Vested and expected to vest, December 31, 2014	1,610,757	$ 25.02	5.7	$ —
Exercisable, December 31, 2014	575,331	$ 30.78	4.4	$ —

The Company utilizes the Black-Scholes valuation model for estimating the fair value of share-based compensation with the following assumptions:

	Nine Months Ended December 31, 2014	Nine Months Ended December 31, 2013
Expected life	4.8 years	4.9 years
Expected volatility	36.4% - 36.6%	43.4% - 43.7%
Expected dividends	4.3% - 4.4%	3.1% - 3.9%
Risk-free rate	1.7%	1.0% - 1.5%

The weighted-average grant date fair value of stock options granted during the nine months ended December 31, 2014 and 2013 was $3.50 and $5.19 per share, respectively.

During the nine months ended December 31, 2014, a total of 459,650 options to purchase shares of common stock were granted under the 2005 Plan at an exercise price equal to the market price of the Company's common stock on the date of grant. A summary of stock options granted under the 2005 Plan during fiscal years 2015 and 2014 is as follows:

Option Grant Date	Number of Shares	Exercise Price	Vesting Terms (1)	Expires
September 2, 2014	20,000	$ 15.63	Five years	September 2, 2022
June 3, 2014	439,650	$ 15.99	Five years	June 3, 2022
Fiscal year 2015 option grants	459,650			
August 15, 2013	85,000	$ 20.85	Five years	August 15, 2021
July 30, 2013	28,000	$ 22.59	Five years	July 30, 2021
May 29, 2013	356,000	$ 17.95	Five years	May 29, 2021
Fiscal year 2014 option grants	469,000			

(1) Options vest in equal annual installments on each grant anniversary date commencing one year following the date of grant.

Employee Share Purchase Plan

On August 11, 2014, the Company's shareholders approved an Employee Share Purchase Plan (the "Purchase Plan") under which 4,000,000 shares of common stock were reserved for future grant. The Purchase Plan allows eligible employees to purchase shares through payroll deductions of up to 15% of total base salary at a price equal to 90% of the lower of the fair market values of the shares as of the beginning or the end of the corresponding offering period. Any shares purchased under the Purchase Plan are subject to a six-month holding period. Employees are limited to purchasing no more than 1,500 shares on any single purchase date and no more than $25,000 in total fair market value of shares during any one calendar year. As of December 31, 2014, the Company has issued 16,305 shares under the Purchase Plan and 3,983,695 shares are available for future issuance. The amount of share-based compensation expense recorded for this plan was insignificant for the nine months ended December 31, 2014.

Employee and Executive Officer Awards

On May 28, 2014, the Board of Directors awarded options to purchase the Company’s common stock to certain high-performing employees. The options were granted on the first day of the next open trading window under the Company's Insider Trading Policy, issued pursuant to the 2005 Plan, have an exercise price equal to the closing price of the Company’s shares on the date of grant, a term of eight years and vest in five equal annual installments commencing one year following the date of grant.

On May 27, 2014, the Compensation Committee of the Board of Directors approved the Company's fiscal year 2015 Executive Compensation Program (the "Program") under which the Company's named executive officers are eligible to receive cash bonuses based on meeting certain target increases in revenue and non-GAAP financial targets, as defined in the Program (i.e. non-GAAP earnings per share and a measure of free cash flow) for fiscal year 2015. Under the Program, the named executive officers also received certain equity incentive awards issued under the 2005 Plan. These equity awards included (i) an aggregate of 105,000 options to purchase the Company's common stock, which were granted on the first day of the next open trading window under the Company's Insider Trading Policy, have an exercise price equal to the closing price of the Company's shares on the date of grant, a term of eight years and a vesting schedule of five equal annual installments commencing one year following the date of grant; and (ii) a potential award of up to an aggregate of 170,000 restricted performance shares of the Company's common stock vesting over a three year period based on the achievement of target average daily share prices for the ninety calendar day period ending May 31st of each of the subsequent three fiscal years.

Share-based compensation expense associated with the restricted performance shares under the Program is based on the grant date fair value measured at the underlying closing share price on the date of grant using a Monte Carlo-based valuation model. Share-based compensation expense associated with the options under the Company’s equity incentive programs are initially based on the number of options expected to vest after assessing the probability that the performance criteria will be met. Cumulative adjustments are recorded quarterly to reflect subsequent changes in the estimated outcome of performance-related conditions. The Company utilizes the Black-Scholes option valuation model with the assumptions in the table below to calculate the share-based compensation expense related to the options. Share-based compensation expense recorded for these performance-based awards was $345 for the nine months ended December 31, 2014 and was insignificant for the nine months ended December 31, 2013.

	Nine Months Ended December 31, 2014	Nine Months Ended December 31, 2013
Expected life	4.8 years	4.9 years
Expected volatility	36.2% - 36.5%	37.7% - 43.5%
Expected dividends	4.3% - 5.0%	3.2% - 3.7%
Risk-free rate	1.6% - 1.8%	1.4% - 1.8%

Non-vested stock option award activity, including employee stock options and performance-based awards, during the nine months ended December 31, 2014 is summarized as follows:

	Non-Vested Number of Shares	Weighted-Average Grant-Date Fair Value per Share
Outstanding, April 1, 2014	991,560	$ 7.73
Granted	459,650	3.50
Vested	(196,790)	8.30
Forfeited/Canceled	(118,075)	7.58
Outstanding, December 31, 2014	1,136,345	$ 5.91

As of December 31, 2014, $5,023 of total unrecognized compensation costs related to stock options is expected to be recognized over a weighted-average period of 3.4 years. This amount does not include the cost of new options that may be granted in future periods or any changes in the Company’s forfeiture percentage. The total fair value of options vested during the nine months ended December 31, 2014 and 2013 was $1,633 and $1,134, respectively.

Director Awards

On May 28, 2014, the Board of Directors approved its 2015 Director Compensation Program, pursuant to which each non-employee director is to be granted shares of restricted stock upon election or re-election to the Board of Directors. The shares of restricted stock are awarded under the 2005 Plan. Such shares of restricted stock vest in two equal, annual installments on the first and second anniversaries of the grant date and are nontransferable for one year following vesting. The weighted-average grant date fair value for the restricted stock was estimated using the market price of the common stock on the date of grant. The fair value of the restricted stock is amortized on a straight-line basis over the vesting period.

The Company recorded compensation expense related to restricted stock of approximately $637 and $473 for the nine months ended December 31, 2014 and 2013, respectively. Restricted stock activity for the nine months ended December 31, 2014 is summarized as follows:

	Number of Shares	Weighted-Average Grant-Date Fair Value per Share
Outstanding, April 1, 2014	64,571	$ 20.74
Granted	48,414	15.77
Vested	(34,113)	21.05
Outstanding, December 31, 2014	78,872	$ 18.13

As of December 31, 2014, $1,000 of total unrecognized compensation costs related to restricted stock is expected to be recognized over a weighted-average period of 1.3 years. This amount does not include the cost of new restricted stock that may be granted in future periods.

10. Concentration of Credit Risk

The Company had cash deposits at U.S. banks and financial institutions which exceeded federally insured limits at December 31, 2014. The Company is exposed to credit loss for amounts in excess of insured limits in the event of non-performance by the institutions; however, the Company does not anticipate non-performance by these institutions.

11. Commitments, Guarantees and Contingencies

Commitments and Guarantees

The Company's software license agreements include a performance guarantee that the Company's software products will substantially operate as described in the applicable program documentation for a period of 365 days after delivery. To date, the Company has not incurred any significant costs associated with its performance guarantee or other related warranties and does not expect to incur significant warranty costs in the future. Therefore, no accrual has been made for potential costs associated with these warranties. Certain arrangements also include performance guarantees related to response time, availability for operational use, and other performance-related guarantees. Certain arrangements also include penalties in the form of maintenance credits should the performance of the software fail to meet the performance guarantees. To date, the Company has not incurred any significant costs associated with these warranties and does not expect to incur significant warranty costs in the future. Therefore, no accrual has been made for potential costs associated with these warranties.

The Company has historically offered short-term rights of return in certain sales arrangements. If the Company is able to estimate returns for these types of arrangements and all other criteria for revenue recognition have been met, revenue is recognized and these arrangements are recorded in the consolidated financial statements. If the Company is unable to estimate returns for these types of arrangements, revenue is not recognized in the consolidated financial statements until the rights of return expire, provided also, that all other criteria of revenue recognition have been met.

Certain standard sales agreements contain a money back guarantee providing for a performance guarantee that is already part of the software license agreement as well as training and support. The money back guarantee also warrants that the software will remain robust and flexible to allow participation in the federal health incentive programs. The specific elements of the performance guarantee pertain to aspects of the software, which the Company has already tested and confirmed to consistently meet using the Company's existing software without any modifications or enhancements. To date, the Company has not incurred any costs associated with this guarantee and does not expect to incur significant costs in the future. Therefore, no accrual has been made for potential costs associated with this guarantee.

The Company's standard sales agreements contain an indemnification provision pursuant to which it shall indemnify, hold harmless, and reimburse the indemnified party for losses suffered or incurred by the indemnified party in connection with any United States patent, any copyright or other intellectual property infringement claim by any third-party with respect to its software. As the Company has not incurred any significant costs to defend lawsuits or settle claims related to these indemnification agreements, the Company believes that its estimated exposure on these agreements is currently minimal. Accordingly, the Company has no liabilities recorded for these indemnification obligations.

Hussein Litigation

On October 7, 2013, a complaint was filed against the Company and certain of the Company’s officers and directors in the Superior Court of the State of California for the County of Orange, captioned Ahmed D. Hussein v. Sheldon Razin, Steven Plochocki, Quality Systems, Inc. and Does 1-10, inclusive, No. 30-2013-00679600-CU-NP-CJC, by Ahmed Hussein, a former director and significant shareholder of the Company. The Company filed a demurrer to the complaint, which the court granted on April 10, 2014. An amended complaint was filed on April 25, 2014. The amended complaint generally alleges fraud and deceit, constructive fraud, negligent misrepresentation and breach of fiduciary duty in connection with statements made to the Company’s shareholders regarding the Company’s financial condition and projected future performance. The amended complaint seeks actual damages, exemplary and punitive damages and costs. The Company filed a demurrer to the amended complaint. On July 29, 2014, the court sustained the demurrer with respect to the breach of fiduciary duty claim, and overruled the demurrer with respect to the fraud and deceit claims. On August 28, 2014, the Company filed an answer and cross-complaint. The Company believes that plaintiff’s claims are without merit and continues to defend against them vigorously.

Federal Securities Class Action

On November 19, 2013, a putative class action complaint was filed on behalf of the shareholders of the Company other than the defendants against the Company and certain of the Company’s officers and directors in the United States District Court for the Central District of California by a shareholder of the Company. After the court appointed lead plaintiffs and lead counsel for this action, and recaptioned the action *In re Quality Systems, Inc. Securities Litigation*, No. 8L13-cv-01818-CJC(JPRx), lead plaintiffs filed an amended complaint on April 7, 2014. The amended complaint, which is substantially similar to the litigation described above under the caption “Hussein Litigation,” generally alleges that statements made to the Company’s shareholders regarding the Company’s financial condition and projected future performance were false and misleading in violation of Section 10(b) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and that the individual defendants are liable for such statements because they are controlling persons under Section 20(a) of the Exchange Act. The complaint seeks compensatory damages, court costs and attorneys' fees. The Company filed a motion to dismiss the amended complaint on June 20, 2014, which the court granted on October 20, 2014, dismissing the complaint with prejudice. Plaintiffs filed a motion for reconsideration of the Court's order, which the court denied on January 5, 2015.

Shareholder Derivative Litigation

On January 24, 2014, a complaint was filed against the Company and certain of the Company’s officers and current and former directors in the United States District Court for the Central District of California, captioned Timothy J. Foss, derivatively on behalf of himself and all others similarly situated, vs. Craig A. Barbarosh, George H. Bristol, James C. Malone, Peter M. Neupert, Morris Panner, D. Russell Pflueger, Steven T. Plochocki, Sheldon Razin, Lance E. Rosenzweig and Quality Systems, Inc., No. SACV14-00110-DOC-JPPx, by Timothy J. Foss, a shareholder of the Company. The complaint arises from the same allegations described above under the captions “Hussein Litigation” and “Federal Securities Class Action” and generally alleges breach of fiduciary duties, abuse of control and gross mismanagement by the Company’s directors, in addition to unjust enrichment and insider selling by individual directors. The complaint seeks compensatory damages, restitution and disgorgement of all profits, court costs, attorneys’ fees and implementation of enhanced corporate governance procedures. The parties have agreed to stay this litigation pending plaintiffs' decision regarding possible appeal in the Federal Securities Class Action. The Company believes that plaintiff’s claims are without merit and intends to defend against them vigorously.

12. Operating Segment Information

The Company has four reportable segments that are evaluated regularly by its chief decision making group (consisting of the Chief Executive Officer, Chief Financial Officer and Chief Operating Officer) in deciding how to allocate resources and in assessing performance. The chief decision making group evaluates performance based upon stand-alone segment operating income. Since assets by segment are not reported to or used by the Company’s chief decision making group to allocate resources, or to assess performance, total assets by segment are not disclosed.

Operating segment data is as follows:

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
Revenue:				
QSI Dental Division	$ 4,480	$ 5,082	$ 13,379	$ 15,137
NextGen Division	92,054	83,881	276,914	250,117
Hospital Solutions Division	4,977	2,483	13,318	12,683
RCM Services Division	21,913	17,408	58,226	51,527
Consolidated revenue	$ 123,424	$ 108,854	$ 361,837	$ 329,464
Operating income (loss):				
QSI Dental Division	$ 1,562	$ 1,323	$ 3,879	$ 4,799
NextGen Division	44,372	36,834	131,983	112,449
Hospital Solutions Division	(838)	(1,969)	(3,272)	(4,661)
RCM Services Division	4,364	2,722	8,932	8,630
Corporate and unallocated	(41,250)	(58,242)	(118,298)	(105,050)
Consolidated operating income (loss)	$ 8,210	$ (19,332)	$ 23,224	$ 16,167

Effective April 1, 2014, the Company refined the measurement of its segment data to better reflect an organizational structure whereby certain expenses managed by functional area leadership are no longer classified within the operating segments but rather as a component of Corporate and unallocated. Such classification is consistent with the disaggregated financial information used by the Company's chief decision making group. The amounts classified as Corporate and unallocated have historically consisted primarily of corporate general and administrative costs and other centrally managed overhead costs, including accounting and finance, human resources, and legal costs, as well as non-recurring acquisition costs and the post-acquisition amortization of certain intangible assets. Currently, as a result of the refinement of its segment data, the Company no longer classifies the costs of the marketing and research and development functional areas and the amortization of capitalized software costs within the operating segments. The Company has retroactively reclassified the prior year operating income in the table above to present all segment information on a comparable basis.

The major components of the Corporate and unallocated amounts are summarized in the table below:

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
Research and development costs	$ 18,468	$ 13,175	$ 51,602	$ 26,404
Amortization of capitalized software costs	3,073	4,050	10,190	9,353
Marketing expense	3,328	2,674	9,439	7,104
Other Corporate and overhead costs (1)	16,381	38,343	47,067	62,189
Total Corporate and unallocated	41,250	58,242	118,298	105,050

(1) Includes the $26.0 million Hospital impairment charge recorded in the three and nine months ended December 31, 2013.

13. Subsequent Events

On January 21, 2015, the Board of Directors approved a quarterly cash dividend of $0.175 per share on the Company’s outstanding shares of common stock, payable to shareholders of record as of March 13, 2015 with an expected distribution date on or about April 3, 2015.

In January 2015, the Company executed a lease amendment to extend the term of the Company's lease at the St. Louis location by 10 years until July 2025. Future minimum lease payments over the term of the amended lease are approximately $6.2 million.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q and certain information incorporated herein by reference contain forward-looking statements within the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. All statements included or incorporated by reference in this Quarterly Report on Form 10-Q, other than statements that are purely historical, are forward-looking statements. Words such as "anticipate," "expect," "intend," "plan," "believe," "seek," "estimate," "will," "should," "would," "could," "may," and similar expressions also identify forward-looking statements. These forward-looking statements include, without limitation, discussions of our product development plans, business strategies, future operations, financial condition and prospects, developments in and the impacts of government regulation and legislation, including, without limitation, The American Recovery and Reinvestment Act ("ARRA") and The Patient Protection and Affordable Care Act, and market factors influencing our results. Our expectations, beliefs, objectives, intentions and strategies regarding our future results are not guarantees of future performance and are subject to risks and uncertainties, both foreseen and unforeseen, that could cause actual results to differ materially from results contemplated in our forward-looking statements. These risks and uncertainties include, but are not limited to, our ability to continue to develop new products and increase systems sales in markets characterized by rapid technological evolution, consolidation, and competition from larger, better-capitalized competitors. Many other economic, competitive, governmental and technological factors could affect our ability to achieve our goals, and interested persons are urged to review any risks that may be described in "Item 1A. Risk Factors" as set forth herein and other risk factors appearing in our most recent Annual Report on Form 10-K for the fiscal year ended March 31, 2014 ("Annual Report"), as supplemented by additional risk factors, if any, in our interim filings on our Quarterly Reports on Form 10-Q, as well as in our other public disclosures and filings with the Securities and Exchange Commission ("SEC"). Because of these risk factors, as well as other variables affecting our financial condition and results of operations, past financial performance may not be a reliable indicator of future performance and historical trends should not be used to anticipate results or trends in future periods. We assume no obligation to update any forward-looking statements. You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of the filing of this Quarterly Report on Form 10-Q.

This management's discussion and analysis of financial condition and results of operations ("MD&A") is provided as a supplement to the consolidated financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q in order to enhance your understanding of our results of operations and financial condition and should be read in conjunction with, and is qualified in its entirety by, the consolidated financial statements and related notes thereto included elsewhere in this Quarterly Report on Form 10-Q. Historical results of operations, percentage margin fluctuations and any trends that may be inferred from the discussion below are not necessarily indicative of the operating results for any future period.

Our MD&A is organized as follows:

- *Management Overview.* This section provides a general description of our Company and operating segments, a discussion as to how we derive our revenue, background information on certain trends and developments affecting our Company and a discussion on management's strategy for driving revenue growth.

- *Critical Accounting Policies and Estimates.* This section discusses those accounting policies that are considered important to the evaluation and reporting of our financial condition and results of operations, and whose application requires us to exercise subjective or complex judgments in making estimates and assumptions. In addition, all of our significant accounting policies, including our critical accounting policies, are summarized in Note 1, "Summary of Significant Accounting Policies," of our notes to consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

- *Company Overview.* This section provides a more detailed description of our Company, its operating segments, a summary of our acquisition transactions and the products and services we offer.

- *Overview of Results of Operations and Results of Operations by Operating Divisions.* These sections provide our analysis and outlook for the significant line items on our consolidated statements of comprehensive income, as well as other information that we deem meaningful to understand our results of operations on both a consolidated basis and an operating division basis.

- *Liquidity and Capital Resources.* This section provides an analysis of our liquidity and cash flows.

- *New Accounting Pronouncements.* This section provides a summary of the most recent authoritative accounting standards and guidance that have either been recently adopted by our Company or may be adopted in the future.

Management Overview

Quality Systems, Inc. and its wholly-owned subsidiaries operate as four business divisions (each, a "Division") which are comprised of: (i) the QSI Dental Division, (ii) the NextGen Division, (iii) the Hospital Solutions Division and (iv) the RCM Services Division. We also have a captive entity in India called Quality Systems India Healthcare Private Limited (“QSIH”). We primarily derive revenue by developing and marketing healthcare information systems that automate certain aspects of medical and dental practices, networks of practices such as physician hospital organizations (“PHOs”) and management service organizations (“MSOs”), ambulatory care centers, community health centers and medical and dental schools along with comprehensive systems implementation, maintenance and support and add on complementary services such as revenue cycle management (“RCM”) and electronic data interchange (“EDI”). Our systems and services provide our clients with the ability to redesign patient care and other workflow processes while improving productivity through the facilitation of managed access to patient information. Utilizing our proprietary software in combination with third-party hardware and software solutions, our products enable the integration of a variety of administrative and clinical information operations. Our scalable interoperability and population health offerings help to improve care collaboration, quality and safety. Enabled by our interoperability solutions, data-driven patient population healthcare management decisions assist in creating more desirable operational, clinical, and financial outcomes that substantiate the value of patient-centered and accountable care models.

The turbulence in the worldwide economy has impacted almost all industries. While healthcare is not immune to economic cycles, we believe it is more heavily influenced by US-based regulatory and national health projects than by the economic cycles of our economy. The impact of the current economic conditions on our existing and prospective clients has been mixed. While we continue to see organizations that are doing fairly well operationally, some organizations, especially those with a large dependency on Medicaid populations, have been impacted by the challenging financial conditions faced by many state governments. Various factors have had, and are anticipated to continue to have, a meaningful impact on the U.S. healthcare industry, including the Obama Administration's broad healthcare reform efforts (particularly the HITECH portion of the American Recovery and Reinvestment Act ("ARRA") and the Patient Protection and Affordable Care Act), the mandate requiring individuals to obtain insurance, the individual state responses to the government-requested Medicaid expansion, the creation and operation of insurance exchanges, and the increasing focus of private businesses on moving their employee health benefit offerings to a more wellness-based health platform.

We have benefited and hope to continue to benefit from the increased demands on healthcare providers for greater efficiency and lower costs, financial incentives from the ARRA to physicians who adopt electronic health records, as well as increased adoption rates for electronic health records and other technology in the healthcare arena. We also believe that healthcare reform and the movement towards pay for performance/quality initiatives will also stimulate demand for robust electronic health record solutions as well as new health information technology solutions from bundled billing capabilities to patient engagement and population health management.

While we expect to benefit from the increasing demands for greater efficiency as well as government support for increased adoption of electronic health records, the market for physician based electronic health records software is becoming increasingly saturated while physician group practices are rapidly being consolidated by hospital, insurance payers and other entities. Hospital software providers are leveraging their position with their hospital customers to gain market share with hospital owned physician practices. Insurance providers and large physician groups are also consolidating physician offices creating additional opportunity for ambulatory software providers like us. Our strategy is to focus on addressing the growing needs of accountable care organizations around interoperability, patient engagements, population health, and data analytics.

We believe that our core strength lies in the central role our software products and services play in the delivery of healthcare by the primary physician in an ambulatory setting. We intend to remain at the forefront of upcoming new regulatory requirements including ICD-10 and meaningful use requirements for stimulus payments. We believe that the expanded requirements for continued eligibility for incentive payments under meaningful use rules will result in an expanded replacement market for electronic health records software. We intend to continue the development and enhancement of our software solutions to support healthcare reform and the transition from fee for service to pay for performance/quality initiatives such as accountable care organizations. Key elements of our future software development will be to expand our interoperability capabilities enhancing the competitiveness of our software offerings, continue to integrate our ambulatory and hospital products, make our products more intuitive and easy to use, and to enhance our ability to deliver our software over the cloud with the latest technology.

We also want to continue investments in our infrastructure, including but not limited to adding new clients through maintaining and expanding sales, marketing and product development activities and expanding our relationship with existing clients through delivery of add-on and complementary products and services while continuing our gold-standard commitment of service in support of our client satisfaction programs. These investments in our infrastructure will continue while maintaining reasonable expense discipline. We believe that our growing customer base that is using our software on a daily basis is a strategic asset, and we intend to leverage this strategic asset by expanding our product and service offerings towards this customer base.

Critical Accounting Policies and Estimates

The discussion and analysis of our consolidated financial statements and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate estimates (including but not limited to those related to revenue recognition, uncollectible accounts receivable, capitalizable software development costs, intangible assets and self-insurance accruals) for reasonableness. We base our estimates on historical experience and on various other assumptions that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that may not be readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We describe our significant accounting policies in Note 2, “Summary of Significant Accounting Policies,” of our notes to consolidated financial statements included in our Annual Report. We discuss our critical accounting policies and estimates in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” of our Annual Report. There have been no material changes in our significant accounting policies or critical accounting policies and estimates since the end of fiscal year 2014.

Company Overview

Quality Systems, Inc. was incorporated in California in 1974. Our principal offices are located at 18111 Von Karman Ave., Suite 700, Irvine, California, 92612. We operate on a fiscal year ending on March 31.

Our Company was founded with an early focus on providing information systems to dental group practices. This focus area would later become the QSI Dental Division. In the mid-1980s, we capitalized on the increasing focus on medical cost containment and further expanded our information processing systems to serve the ambulatory market. In the mid-1990s, we made two acquisitions that accelerated our penetration of the ambulatory market and formed the basis for the NextGen Division. In the last few years, we acquired several companies as part of our strategy to enhance our EDI and RCM services capabilities as well as expand into the small and specialty hospital market. More recently, we acquired Mirth Corporation ("Mirth"), which operates under the NextGen Division, and is expected to enhance our current enterprise interoperability initiatives and broaden our accountable and collaborative care, population health, disease management and clinical data exchange offerings. Today, we serve the dental, ambulatory, hospital and RCM services markets through our QSI Dental Division, NextGen Division, Hospital Solutions Division and RCM Services Division.

The Divisions have historically operated as stand-alone operations, with each Division maintaining its own distinct product lines, product platforms, development, implementation and support teams and branding. However, there are a growing number of customers who are simultaneously utilizing software or services from more than one of our Divisions. In an effort to encourage this cross selling of our products and services between Divisions, we are in the process of further integrating our ambulatory and hospital products to provide a more robust and comprehensive platform to offer our customers. The Divisions also share the resources of our “corporate office,” which includes a variety of accounting and other administrative functions.

In September 2012, we announced certain organizational changes to achieve greater efficiency and integration in our operations as well as to enhance our ability to cross sell products and services to our customers. The changes consolidated Sales, Marketing, Information Technology, and Software Development responsibilities into separate Company-wide roles. We also announced the hiring of a Chief Operating Officer, reporting directly to the Chief Executive Officer, responsible for the operations of the Company across all Divisions. We are continuing to evaluate the organizational structure of the Company with the objective to achieve greater synergies and further integration of our products and services, including software implementation and customer support functions.

The QSI Dental Division, NextGen Division and Hospital Solutions Division develop and market software that is designed to automate and streamline a number of the administrative functions required for operating a medical, dental, or hospital practice, such as patient scheduling and billing. It is important to note that since in both the medical and dental environments, practice management software systems have already been implemented by the vast majority of practices, we actively compete in a replacement market by leveraging the benefits of our interoperable electronic health records software. With the addition of Mirth, our combined solutions enrich the already strong collaborative, connected care support and set the stage for data synchronization, interoperability growth and expansion of our current accountable and collaborative care, population health, disease management and clinical data exchange offering. These Divisions also develop and market software that automates patient records in physician practices, community health centers and hospital settings. In this patient records area of our business, we are typically competing to replace paper-based patient record alternatives as opposed to replacing previously purchased systems. The Hospital Solutions Division develops and markets financial management and billing software products, which perform administrative functions required for operating small and specialty hospitals as well as clinical offerings such as multi-disciplinary clinical documentation and computerized physician order entry. The RCM Services Division provides technology solutions and outsourcing services to cover the full spectrum of healthcare providers' RCM needs, with a primary focus on outsourced billing and collection services.

In January 2011, QSIH was formed in Bangalore, India to function as our India-based captive to offshore technology application development and business processing services. Our employee base in Bangalore has since grown to over 300 employees with a primary focus on software development activities.

We continue to pursue product and service enhancement initiatives within each of our Divisions. The majority of such expenditures are currently targeted to the product lines and client base of the NextGen Division.

The following table reflects our reported segment revenue and segment revenue growth (decline) by Division for the three and nine months ended December 31, 2014 and 2013:

	Segment Revenue Breakdown			
	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
QSI Dental Division	3.6%	4.7%	3.7%	4.6%
NextGen Division	74.6%	77.0%	76.5%	76.0%
Hospital Solutions Division	4.0%	2.3%	3.7%	3.8%
RCM Services Division	17.8%	16.0%	16.1%	15.6%
Consolidated	100.0%	100.0%	100.0%	100.0%

	Segment Revenue Growth (Decline)			
	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
QSI Dental Division	(11.8)%	(0.1)%	(11.6)%	1.7 %
NextGen Division	9.7 %	(2.2)%	10.7 %	(3.5)%
Hospital Solutions Division	100.4 %	(66.3)%	5.0 %	(52.9)%
RCM Services Division	25.9 %	6.8 %	13.0 %	7.6 %
Consolidated	13.4 %	(4.9)%	9.8 %	(5.6)%

QSI Dental Division. The QSI Dental Division, co-located with our corporate headquarters in Irvine, California, focuses on developing, marketing and supporting software suites sold to dental group organizations located throughout the United States. The QSI Dental Division sells additional licenses to its legacy products as existing clients expand their operations, and sells its cloud-based Software as a Service ("SaaS") model practice management and clinical software solutions to new and existing customers. This software solution, QSIDental Web ("QDW"), is marketed primarily to multi-location dental group practices in which the QSI Dental Division has historically been a dominant player. QDW offers a lower cost of ownership as it is a cloud-based solution that requires a customer to have Internet access to run the application. Further, QSI Dental sells its Electronic Dental Chart in conjunction with NextGen PM and EHR ("Electronic Health Record") and is marketed as NextGen® EDR (“Electronic Dental Record”) to Federally Qualified Health Centers (“FQHC”) and other safety net entities further defined below.

The QSI Dental Division participates jointly with the NextGen Division in providing software and services to safety-net clinics like FQHCs and other “safety net” health centers, including Public Health Centers, Community Health Centers, Free Clinics, as well as Rural and Tribal Health Centers. FQHCs are community-based organizations and are funded by the federal government, which provide medical and dental services to underprivileged and underserved communities. The Patient Protection and Affordable Care Act, which was signed into law in March 2010, reserved $11 billion over a multi-year period for FQHCs, creating unprecedented opportunities for FQHCs growth and the formation of new FQHCs. When combined and used in tandem, NextGen® EHR, NextGen® EDR, and NextGen® PM provide a unique product in this marketplace — an integrated patient record accessible by both physicians and dentists. On May 3, 2013, NextGen® EDR version 4.3 was ONC-ATCB certified by the Certification Commission for Health Information ("CCHIT®") as a complete EHR and complies with all clinical quality measures for Eligible Providers. The additional software NextGen® EDR version 4.3 relied on to demonstrate compliance was NextGen® EHR version 5.8.

The QSI Dental Division's legacy practice management software suite uses a UNIX® operating system. It's Clinical Product Suite (“CPS”) can be fully integrated with the client server-based practice management software offered from each of our Divisions. When integrated and delivered with the NextGen® PM solution, CPS is re-branded as NextGen® EDR. CPS/EDR incorporates a wide range of clinical tools including, but not limited to, periodontal charting and digital imaging of X-ray and inter-oral camera images as part of the electronic patient record. The QSI Dental Division also develops, markets, and provides EDI services to dental practices, including electronic submission of claims to insurance providers as well as automated patient statements.

On November 14, 2011 we acquired ViaTrack, a developer and provider of information technologies that enhance EDI offerings. This acquisition provides a platform to pursue significant opportunities that exist to leverage ViaTrack's technologies to reduce costs and enhance our EDI offerings to all divisions. ViaTrack's operations are managed under the QSI Dental Division and its revenues and costs are reflected within the operating results of the respective divisions that derive benefit from the sales of ViaTrack products.

NextGen Division. The NextGen Division, with headquarters in Horsham, Pennsylvania and a significant location in Atlanta, Georgia, provides integrated clinical, financial and connectivity solutions for ambulatory and dental provider organizations. The NextGen Division's major product categories include the NextGen® Ambulatory product suite and NextGen® Community Connectivity.

The NextGen Ambulatory product suite streamlines patient care with standardized, real-time clinical and administrative workflows within a physician’s practice, and major product categories include NextGen® EHR, NextGen® PM, NextGen® Dashboard, NextGen® Mobile, and NextGen® NextPen. NextGen® Community Connectivity consists of NextGen® Health Information Exchange (formerly Community Health Solution), NextGen® Patient Portal (NextMD.com), and NextGen® Health Quality Measures. The NextGen Division also offers hosting services, NextGuard – Data Protection services, and consulting services, such as strategic governance models and operational transformation, technical consulting such as data conversions or interface development. The NextGen Division products utilize Microsoft Windows technology and can operate in a client-server environment as well as via private intranet, the Internet, or in an ASP environment. The NextGen Division also provides EDI services, which include electronic submission of claims to insurance providers as well as automated patient statements.

On September 9, 2013, we acquired Mirth, a global leader in health information technology that helps clients achieve interoperability. Operating results associated with Mirth products and services are included in the NextGen Division. The acquisition of Mirth will enhance our current enterprise interoperability initiatives and broaden our accountable and collaborative care, population health, disease management and clinical data exchange offerings. Mirth offers a wide variety of products and services utilized by both users of Mirth open code technology as well as a large base of domestic and international paying customers. Product offerings available from Mirth include Mirth Connect, Mirth Results, Mirth Match, Mirth Mail, Mirth Appliance, Mirth Care and Mirth Gateway. As a direct result of the Mirth acquisition, we introduced NextGen® Share to our customer base in November 2013. As our first offering that integrates technologies from both NextGen Healthcare and Mirth, NextGen® Share provides the ability to securely and easily share patient charts and other data with other practices using NextGen Internet based software.

Hospital Solutions Division. The Hospital Solutions Division, with its primary location in Austin, Texas, provides integrated clinical, financial and connectivity solutions for rural, community and specialty hospitals. This Hospital Solutions Division also develops and markets an equivalent revenue cycle management and clinical information systems software products for the small and specialty hospital market, which perform the administrative functions required for operating hospitals.

We have acquired companies that were established developers of software and services for the hospital market to operate under the Hospital Solutions Division. On May 1, 2012, we acquired The Poseidon Group, a provider of emergency department software. On July 26, 2011, we acquired CQI Solutions, Inc., a provider of hospital systems for surgery management. On April 29, 2011, we acquired IntraNexus, Inc., a provider of Web-based integrated clinical and hospital information systems. On February 10, 2010, we acquired Opus Healthcare Solutions, LLC, a provider of Web-based clinical solutions to hospital systems and integrated health networks nationwide and on August 12, 2009 we acquired Sphere Health Systems, Inc., a provider of financial information systems to the small hospital inpatient market. These acquisitions are part of our long term strategy to expand in the small and specialty hospital market and to add new clients by taking advantage of cross selling opportunities between the ambulatory and hospital markets.

RCM Services Division. The RCM Services Division, with locations in St. Louis, Missouri, North Canton, Ohio, South Jordan, Utah and Hunt Valley, Maryland, provides technology solutions and consulting services to cover the full spectrum of healthcare providers' RCM needs, from patient access through claims denials, with a primary focus on billing and collection services. The RCM Services Division combines a Web-delivered SaaS model and the NextGen® PM software platform to execute its service offerings. Execution of the plan to transition our client base onto the NextGen platform is being implemented. On April 15, 2012, we acquired Matrix Management Solutions, LLC ("Matrix"). Since 1998, North Canton, Ohio-based Matrix, a value-added reseller for NextGen Healthcare, has provided RCM services, healthcare information technology solutions and training, implementation and support centered on NextGen technology, to its clients nationwide. The acquisition has enabled our RCM Services Division to expand its footprint among private and hospital-based physicians and groups by leveraging Matrix's RCM expertise.

Overview of Our Results

- Consolidated revenue increased 9.8% in the nine months ended December 31, 2014 as compared to the prior year period. The increase reflects a 13.3% increase in recurring services revenue (i.e. maintenance, EDI, RCM and other services revenues), partially offset by a 4.3% decrease in system sales revenue. The increase in recurring services revenue is due to an increase across all categories of recurring services, including a substantial increase in subscription revenue of $12.8 million in the nine months ended December 31, 2014 as compared to the prior year period. Subscription revenue included in other revenue was $31.3 million in the nine months ended December 31, 2014 versus $18.4 million in the same prior year period. The increase in subscription revenue reflects increases in Mirth related interoperability subscription revenue as well as increases in subscription revenue related to our NextGen Patient Portal product offering. The decline in system sales revenue reflects the increasingly saturated markets in which our core software products are sold.
- For the nine months ended December 31, 2014, recurring services revenue comprised 82.8% of consolidated revenue, as compared to 80.2% in the prior year period.
- Consolidated gross profit as a percentage of revenue increased to 53.8% for the nine months ended December 31, 2014 compared to 49.4% in the prior year period. The change is primarily the result of $20.1 million in impairment charges recorded to cost of software revenue in the prior year period.
- Consolidated operating income increased 43.7%, or $7.1 million, in the nine months ended December 31, 2014 as compared to the prior year period. The increase is mostly the result of $20.1 million and $5.9 million in Hospital impairment charges recorded in the prior year period to cost of revenue and operating expenses, respectively, which was offset by a substantial increase of $25.2 million in research and development costs as compared to the prior year period resulting from both higher gross expenditures and lower capitalization rates of software development costs due to shorter development cycles. Refer to the table below in the "Corporate and unallocated amounts" section for a comparative analysis of gross expenditures and capitalized software costs.

QSI Dental Division

- QSI Dental Division revenue decreased 11.6% in the nine months ended December 31, 2014. Divisional operating income (excluding Corporate and unallocated amounts) was $3.9 million in the nine months ended December 31, 2014, a decrease of 19.2% as compared to the same prior year period. The decrease in operating income was primarily the result of a $1.6 million decrease in system sales revenue. It should be noted that the division's current cloud-based software solution, QDW, is being sold primarily as a SaaS solution for which revenue is recognized over an extended period of time rather than upfront, which has resulted in a recent decline to divisional system sales revenues. Revenue recognized from QDW was approximately $0.7 million in the nine months ended December 31, 2014 as compared to $0.5 million in the same prior year period.
- The QSI Dental Division is well-positioned to sell to the FQHCs market and intends to continue leveraging the NextGen Division's sales force to sell its dental electronic medical records software to practices that provide both medical and dental services, such as FQHCs, which are receiving grants as part of the ARRA.
- Our goal for the QSI Dental Division is to continue to invest in the new cloud-based QDW platform while aggressively marketing QDW to both new and existing customers. The company is in the early stages of implementing QDW to several key customers of the QSI Dental Division.

NextGen Division

- NextGen Division revenue increased 10.7% in the nine months ended December 31, 2014, as compared to the same prior year period. This variance reflects a 15.2% growth in recurring service revenue, including an increase of 7.4% in maintenance, 13.8% in EDI revenue and 36.3% in other services revenue. The significant growth in other services revenue was driven by a 77.8% growth in subscriptions as compared to the same prior year period. As noted above, subscriptions revenue growth was due to increases in Mirth related interoperability subscription revenue as well as increases in subscription revenue related to our patient portal product offering. Recurring service revenue increased to $220.7 million and accounted for 79.7% of total NextGen Division revenue for the nine months ended December 31, 2014. In the same period a year ago, recurring service revenue of $191.5 million represented 76.6% of total NextGen Division revenue.
- NextGen Division operating income (excluding Corporate and unallocated amounts) increased by 17.4% in the nine months ended December 31, 2014, as compared to the same prior year period. The increase in operating income is primarily the result of the increase in total revenue and a 12.5% decline in overall operating expenses, including decreases in sales commissions and bad debt expense. Sales commissions decreased, despite an increase in total divisional revenue, due to the change in revenue mix towards recurring service revenue, which has a lower commissions rate than system sales. Bad debt expense has decreased as a result of improved collections from greater emphasis on working capital management.
- Our goals include taking maximum advantage of benefits related to the ARRA and continuing to further enhance our existing products, including continued efforts to

maintain our status as a qualified vendor under the ARRA, expanding our software and service offerings supporting pay-for-performance initiatives around accountable care organizations, bringing greater ease of use and intuitiveness to our software products, expanding our interoperability capabilities, integrating our hospital and ambulatory software products and further development and enhancements of our portfolio of specialty focused templates within our EHR software. We intend to remain at the forefront of upcoming new regulatory requirements, including ICD-10 and meaningful use requirements for stimulus payments. We believe that the expanded requirements for continued eligibility for incentive payments under meaningful use rules will result in an expanded replacement market for electronic health records software. We also intend to continue selling additional software and services to existing clients, expanding penetration of connectivity and other services to new and existing clients, and capitalizing on growth and cross selling opportunities within the RCM Services Division. We believe that our acquisition of Mirth will provide improved capabilities around interoperability and improved competitiveness in our markets, as well as providing new customers and expanded markets for the NextGen Division.

- The NextGen Division's growth is attributed to a strong brand name and reputation within the marketplace for healthcare information technology software and services and investments in sales and marketing activities, including new marketing campaigns, Internet advertising investments, trade show attendance and other expanded advertising and marketing expenditures. We have also recently expanded our relationship with certain value added resellers with significant resources both domestically and internationally.

Hospital Solutions Division

- Hospital Solutions Division revenue increased 5.0% in the nine months ended December 31, 2014. Revenue was positively impacted by a 40.6% increase in system sales, partially offset by a 4.2% decline in recurring service revenue. The significant increase in system sales is primarily reflective of lower sales returns and related reserves in the current period.

- Divisional operating loss (excluding Corporate and unallocated amounts) was $3.3 million for the nine months ended December 31, 2014 as compared to a $4.7 million loss for the same prior year period. The improvement in operating results is due to an increase in gross profit, driven by the increase in system sales noted above.

- The Hospital Solutions Division has incurred losses in the last several quarters and is expected to continue to incur losses for the foreseeable future while we continue to invest in and support our existing customer base. Our expectations about the future performance of this Division resulted in the full impairment of significant long-term assets of this Division during the three months ended December 31, 2013. Along with recording the impairment charge, we have also ceased capitalization and amortization of software development costs related to the Hospital Solutions Division's software products.

RCM Services Division

- RCM Services Division revenue increased 13.0% in the nine months ended December 31, 2014. The RCM Services Division benefited mostly from new clients added during the nine months ended December 31, 2014 as well as organic growth achieved through cross selling RCM services to existing NextGen Division clients.

- Operating income increased 3.5% in the nine months ended December 31, 2014 as compared to the same prior year period due primarily to an increase in divisional gross profit compared to the prior year period.

- The Company believes that a significant opportunity exists to continue cross selling RCM services to existing customers. The portion of existing NextGen customers who are using the RCM Services Division's services is less than 10%. Management is actively pursuing efforts to achieve faster growth from expanded efforts to leverage the existing NextGen Division's sales force towards selling RCM services. We also believe that the increased complexity related to the billing and collections process, expected to go into effect with ICD-10, will create additional opportunities for our RCM Services Division.

- Actual and expected customer turnover may impact short term revenue for the division. However, we are encouraged by our RCM sales pipeline and increasing sales activity.

Corporate and unallocated amounts (costs not allocated to the operating segments)

- Effective April 1, 2014, we refined the measurement of our segment data to better reflect an organizational structure whereby certain expenses managed by functional area leadership are no longer classified within the operating segments but rather as a component of Corporate and unallocated. Such classification is consistent with the disaggregated financial information used by the chief decision making group. As a result, we no longer classify the amortization of capitalized software costs within the operating segments. The Company has retroactively reclassified the prior year gross margin amounts included in the MD&A to present all segment information on a comparable basis. For additional details, refer to Note 12, "Operating Segment Information," of our notes to consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

- Research and development costs increased by 95.4% to $51.6 million for the nine months ended December 31, 2014 as compared to $26.4 million for the same prior year period due primarily to a reduction in the capitalization rate of software costs due to shorter development cycles as well as higher gross expenditures on research and development. We anticipate an increase in gross research and development expenditures including both amounts expensed and capitalized due to a growing rate of investment to concurrently develop major new products while continuing to create significant new enhancements to our existing product lines. As we release the next major version of our flagship software platform, expected to occur during fiscal 2016, we expect a decline in the amount of software cost capitalization related to this product. Additionally, we have noted a trend towards a more agile development approach that inherently shortens the time frame during which development costs may be capitalized and impacts our capitalization rate of software. Although lower capitalization rates have no impact on our overall cash flows, it results in a higher portion of our software development costs being expensed up front, resulting in increased research and development costs as compared to prior periods. As summarized in the table below, the amount of software costs capitalized in proportion to the amount of total research and development expenditures, including both amounts expensed and capitalized, has declined significantly for the three and nine months ended December 31, 2014 as compared to the same prior year periods:

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2014	2013	2014	2013
Gross expenditures	$ 21,634	$ 16,794	$ 61,137	$ 45,318
Capitalized software costs	(3,166)	(3,619)	(9,535)	(18,914)
Research and development costs, as reported	$ 18,468	$ 13,175	$ 51,602	$ 26,404
Capitalized software costs as a percentage of gross expenditures	14.6%	21.5%	15.6%	41.7%

- Amortization of capitalized software costs increased by 8.9% to $10.2 million for the nine months ended December 31, 2014 as compared to $9.4 million for the same prior year period. The increase in amortization of capitalized software costs is due to the general release of the latest significant versions of our ambulatory software products during the third quarter of fiscal 2014. We expect that these releases along with the upcoming general release of the next major version of our flagship software platform expected to occur during fiscal 2016 will result in even significantly higher rates of amortization relative to previously capitalized software development costs reflected in our recent historical operating results. Amortization of capitalized software costs are reflected as cost of revenue on our consolidated statements of comprehensive income. Refer to Note 5, "Capitalized Software Costs" of our notes to the consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q for an estimate of future amortization of capitalized software costs.

- Other Corporate and overhead costs decreased by $15.1 million to $47.1 million for the nine months ended December 31, 2014 as compared to $62.2 million for the same prior year period primarily due to the $26.0 million Hospital impairment charge recorded in the prior year period, partially offset by increases in salaries and benefits, legal expense, and acquisition related costs. In addition, an increase in marketing headcount plus added utilization of online advertising and media placement has resulted in a 32.9% increase in marketing expense to $9.4 million for the nine months ended December 31, 2014 as compared to $7.1 million for the same prior year period.

The following table sets forth, for the periods indicated, the percentage of net revenue represented by each item in our consolidated statements of comprehensive income (loss) (certain percentages below may not sum due to rounding):

(Unaudited)	Three Months Ended December 31, 2014	Three Months Ended December 31, 2013	Nine Months Ended December 31, 2014	Nine Months Ended December 31, 2013
Revenues:				
Software and hardware	13.2%	13.0 %	12.5%	13.9%
Implementation and training services	3.0	4.6	4.7	5.9
System sales	16.2	17.6	17.2	19.8
Maintenance	34.9	36.5	34.8	36.0
Electronic data interchange services	15.4	15.3	15.6	15.1
Revenue cycle management and related services	16.5	14.9	15.1	14.5
Other services	17.0	15.7	17.4	14.6
Maintenance, EDI, RCM and other services	83.8	82.4	82.8	80.2
Total revenues	100.0	100.0	100.0	100.0
Cost of revenue:				
Software and hardware	5.0	25.2	5.3	11.3
Implementation and training services	3.7	6.9	5.1	6.5
Total cost of system sales	8.7	32.1	10.4	17.8
Maintenance	6.0	5.2	5.8	4.9
Electronic data interchange services	9.7	9.4	9.9	9.6
Revenue cycle management and related services	11.5	10.8	11.1	10.4
Other services	8.2	7.8	9.0	7.9
Total cost of maintenance, EDI, RCM and other services	35.4	33.2	35.8	32.8
Total cost of revenue	44.0	65.3	46.2	50.6
Gross profit	56.0	34.7	53.8	49.4
Operating expenses:				
Selling, general and administrative	33.6	33.9	32.3	33.6
Research and development costs	15.0	12.1	14.3	8.0
Amortization of acquired intangible assets	0.7	1.1	0.8	1.1
Total operating expenses	49.3	52.5	47.4	44.5
Income (loss) from operations	6.7	(17.8)	6.4	4.9
Interest income (expense), net	(0.1)	0.1	0.0	0.0
Other income (expense), net	0.0	0.0	0.0	(0.1)
Income (loss) before income taxes	6.6	(17.7)	6.4	4.8
Provision for (benefit of) income taxes	1.2	(6.1)	1.8	1.6
Net income (loss)	5.4%	(11.6)%	4.6%	3.2%

Comparison of the Three Months Ended December 31, 2014 and December 31, 2013

Net Income/Loss. Our net income for the three months ended December 31, 2014 was $6.7 million, or $0.11 per share on both a basic and fully diluted basis. In comparison, we had a net loss of $12.6 million, or $0.21 per share, on both a basic and fully diluted basis for the three months ended December 31, 2013. The change in net income for the three months ended December 31, 2014 was primarily attributed to the following:

- the prior year period included a $26.0 million impairment charge related to our Hospital Solutions Division while the current period does not include any such impairment charge
- software sales in the current quarter increased by $2.6 million, or 21.3%, as a result of increased software license sales combined with a $1.7 million reduction in reserves for sales returns during the current period
- recurring revenue streams including maintenance, RCM, EDI and other grew $13.7 million, or 15.3%, compared to the prior year period
- these positive contributions to net income were offset by a $5.3 million increase in research and development expenses in the current period primarily due to higher gross expenditures in conjunction with lower capitalization rates of software development costs as well as a $4.6 million increase in other selling, general and administrative costs and an increase of $8.1 million in the provision for income taxes, principally reflecting the net loss and deductibility of a portion of the impairment charge in the prior year period.

Revenue. Revenue for the three months ended December 31, 2014 increased 13.4% to $123.4 million from $108.9 million for the three months ended December 31, 2013. NextGen Division revenue increased 9.7% to $92.1 million compared to $83.9 million in the three months ended December 31, 2013, RCM Services Division revenue increased 25.9% to $21.9 million from $17.4 million, and the Hospital Solutions Division revenue increased 100.5% during that same period to $5.0 million from $2.5 million. Revenue for the QSI Dental Division decreased 11.9% to $4.5 million from $5.1 million compared to the same prior year period.

System Sales. Revenue from consolidated system sales for the three months ended December 31, 2014 increased 4.4% to $20.0 million from $19.2 million in the same prior year period.

The following table breaks down our reported system sales into software, hardware and third party software, and implementation and training services components on a consolidated and divisional basis for the three months ended December 31, 2014 and 2013 (in thousands):

	Software	Hardware and Third Party Software	Implementation and Training Services	Total System Sales
Three Months Ended December 31, 2014				
QSI Dental Division	$ 149	$ 199	$ 238	$ 586

NextGen Division	13,109	1,152	3,183	17,444
Hospital Solutions Division	1,594	26	116	1,736
RCM Services Division	106	4	121	231
Consolidated	$ 14,958	$ 1,381	$ 3,658	$ 19,997
Three Months Ended December 31, 2013				
QSI Dental Division	$ 650	$ 382	$ 256	$ 1,288
NextGen Division	13,530	1,118	3,652	18,300
Hospital Solutions Division	(1,951)	287	1,138	(526)
RCM Services Division	98	—	—	98
Consolidated	$ 12,327	$ 1,787	$ 5,046	$ 19,160

The overall increase in system sales was driven mostly by an increase of $2.3 million for the Hospital Solutions Division in the three months ended December 31, 2014 versus the same period last year. Software sales for the division increased $3.5 million due primarily to a decline in software sales credits and related reserves, partially offset by a $1.0 million decrease in implementation and training services related to the recent decline in new software sales.

System sales for the NextGen Division declined by $0.9 million due to a 3.1% decrease in software license revenue and 12.8% decrease in implementation and training services during the three months ended December 31, 2014 versus the same period last year, resulting from lower sales to both new and existing customers. The NextGen Division’s software revenue accounted for 75.1% of divisional system sales revenue during the three months ended December 31, 2014 compared to 73.9% during the same period a year ago. Software license revenue continues to be an area of primary emphasis for the NextGen Division.

Total system sales for the QSI Dental Division decreased 54.5% in the three months ended December 31, 2014 versus the same period last year, partially because the division's current software solution, QDW, is being sold primarily as a SaaS solution for which revenue is recognized over an extended period of time as other services revenue rather than upfront as software revenue.

We believe there are other trends which may positively impact future systems sales. Many of our existing large enterprise customers have plans to grow, which will create future revenue opportunities as these customers purchase additional software and services to support their growth plans. We also expect to benefit from the growth of a replacement market driven by an expected consolidation of electronic health records vendors. Finally, we believe many new opportunities will be created by the evolution of healthcare from a pay for services reimbursement model to a pay for performance model around the management of patient populations. Additionally, the Mirth acquisition provided us with new products and services around HIE and interoperability, which we intend to utilize to drive future growth. It is difficult to assess the relative impact as well as the timing of positive and negative trends, however, we believe we are well positioned to support the ever increasing need for healthcare information technology.

During the three months ended December 31, 2014, 6.9% of consolidated system sales revenue was represented by hardware and third party software as compared to 9.3% during the same period a year ago. The number of clients who purchase hardware and third party software and the dollar amount of hardware and third party software revenue fluctuates each quarter depending on the needs of clients. The inclusion of hardware and third party software in our sales arrangements is typically at the request of our clients.

Implementation and training revenue related to system sales at the NextGen Division declined 12.8% in the three months ended December 31, 2014 as compared to the same prior year period while implementation and training revenue at the QSI Dental Division decreased 7.0% in the three months ended December 31, 2014 compared to the same prior year period. Implementation and training revenue related to system sales at the Hospital Solutions Division decreased 89.8%, in the three months ended December 31, 2014 as compared to the same prior year period.

The amount of implementation and training services revenue is dependent on several factors, including timing of client implementations, the availability of qualified staff and the mix of services being rendered. It should be noted that we have experienced a decline in the level of systems sales in recent quarters which in turn have resulted in a decline in the amount of implementation services sold. However, we believe that the demand for services is going to increase especially as our customers implement the newest release of our core ambulatory software products, which support new ICD-10 billing requirements.

Maintenance, EDI, RCM and Other Services. For the three months ended December 31, 2014, our consolidated revenue from maintenance, EDI, RCM and other services grew 15.3% to $103.4 million from $89.7 million in the same prior year period. The increase is due to growth across all categories of recurring service revenue.

The following table details maintenance, EDI, RCM and other services revenue by category on a consolidated and divisional basis for the three months ended December 31, 2014 and 2013 (in thousands):

	Maintenance	EDI	RCM	Other	Total
Three Months Ended December 31, 2014					
QSI Dental Division	$ 2,166	$ 1,178	$ —	$ 550	$ 3,894
NextGen Division	38,285	17,633	—	18,692	74,610
Hospital Solutions Division	2,442	24	—	775	3,241
RCM Services Division	152	216	20,392	922	21,682
Consolidated	$ 43,045	$ 19,051	$ 20,392	$ 20,939	$ 103,427
Three Months Ended December 31, 2013					
QSI Dental Division	$ 2,090	$ 1,328	$ —	$ 376	$ 3,794
NextGen Division	35,343	15,242	—	14,996	65,581
Hospital Solutions Division	2,187	37	—	785	3,009
RCM Services Division	143	30	16,178	959	17,310
Consolidated	$ 39,763	$ 16,637	$ 16,178	$ 17,116	$ 89,694

Total category revenue at the NextGen Division for the three months ended December 31, 2014 increased by 13.8% to $74.6 million from $65.6 million for the same prior year period. NextGen Division maintenance revenue for the three months ended December 31, 2014 grew 8.3% to $38.3 million from $35.3 million for the same prior year period primarily as a result of net additional licenses from both new and existing clients. NextGen Division EDI revenue grew 15.7% to $17.6 million compared to $15.2 million in the same prior year period. The growth in NextGen EDI revenue has come from new clients and from further penetration of the division's existing client base. Other services revenue for the NextGen Division, which consists primarily of third party annual software license renewals, consulting services, SaaS fees, hosting services, and other subscriptions, increased 24.6% to $18.7 million in the three months ended December 31, 2014 from $15.0 million in the same prior year period. Other services revenue benefited significantly from a $3.9 million increase in customer subscriptions.

For the three months ended December 31, 2014, RCM revenue for the RCM Services Division increased to $20.4 million compared to $16.2 million in the same prior year period. The growth in RCM revenue is primarily attributable to organic growth achieved through cross selling RCM services to existing NextGen Division clients as well as the addition of new clients. For the Hospital Solutions Division, maintenance, EDI and other services revenue for the three months ended December 31, 2014 increased 7.7% as compared to the same prior year period primarily due to a decline in sales returns related to maintenance revenue. QSI Dental Division maintenance, EDI and other services revenue for the three months ended December 31, 2014 and 2013 increased 2.6% compared to the same prior year period due mostly to growth of subscription revenues related to QDW.

We intend to continue promoting recurring maintenance, EDI and RCM services to both new and existing clients.

Cost of Revenue. Cost of revenue for the three months ended December 31, 2014 decreased to $54.4 million from $71.1 million in the same prior year period and the cost of revenue as a percentage of revenue decreased to 44.0% from 65.3%. The decrease in cost of revenue as a percentage of revenue is primarily due to the $20.1 million Hospital impairment charge recorded to cost of software revenue in the prior year period, which is partially offset by an increase in cost of revenue related to a change in the mix of revenues toward recurring services revenue, which have historically experienced a lower profit margin than system sales. For the three months ended December 31, 2014, recurring services revenue comprised 83.8% of consolidated revenue, as compared to 82.4% in the prior year period.

The following table details revenue and cost of revenue on a consolidated and divisional basis for the three months ended December 31, 2014 and 2013 (in thousands):

	Three Months Ended December 31,			
	2014	%	2013	%
QSI Dental Division				
Revenue	$ 4,480	100.0%	$ 5,082	100.0 %
Cost of revenue	2,114	47.2%	2,392	47.1 %
Gross profit	$ 2,366	52.8%	$ 2,690	52.9 %
NextGen Division				
Revenue	$ 92,054	100.0%	$ 83,881	100.0 %
Cost of revenue	30,678	33.3%	27,340	32.6 %
Gross profit	$ 61,376	66.7%	$ 56,541	67.4 %
Hospital Solutions Division				
Revenue	$ 4,977	100.0%	$ 2,483	100.0 %
Cost of revenue	2,954	59.4%	4,869	196.1 %
Gross profit (loss)	$ 2,023	40.6%	$ (2,386)	(96.1)%
RCM Services Division				
Revenue	$ 21,913	100.0%	$ 17,408	100.0 %
Cost of revenue	14,757	67.3%	12,130	69.7 %
Gross profit	$ 7,156	32.7%	$ 5,278	30.3 %
Unallocated cost of revenue	$ 3,857	N/A	$ 24,324	N/A
Consolidated				
Revenue	$ 123,424	100.0%	$ 108,854	100.0 %
Cost of revenue	54,360	44.0%	71,055	65.3 %
Gross profit	$ 69,064	56.0%	$ 37,799	34.7 %

Gross profit margin for the NextGen Division decreased for the three months ended December 31, 2014 compared to the same prior year period primarily due to a decrease in high-margin software sales. Gross profit margin for the RCM Services Division increased compared to the same prior year period primarily as a result of increased cash collections from customers for which revenues are being recognized on a cash collection basis and the related costs of revenue have been previously incurred. The gross profit (loss) margin for the Hospital Solutions Division in the three months ended December 31, 2014 benefited from higher system sales, resulting from lower software returns and related reserves in the current period, combined with a decline in cost of revenue due mostly to lower payroll and related benefits costs. The decrease in unallocated cost of revenue is primarily due to the $20.1 million Hospital impairment charge recorded in the prior year period.

The following table details the individual components of cost of revenue and gross profit (loss) as a percentage of total revenue on a consolidated and divisional basis for the three months ended December 31, 2014 and 2013:

	Software	Hardware and Third Party Software	Payroll and Related Benefits	EDI	Other	Total Cost of Revenue	Gross Profit (Loss)
Three Months Ended December 31, 2014							
QSI Dental Division	0.0%	3.8%	26.5%	8.3%	8.6%	47.2%	52.8 %
NextGen Division	1.3%	1.0%	13.2%	11.4%	6.4%	33.3%	66.7 %
Hospital Solutions Division	0.0%	0.1%	49.5%	0.4%	9.4%	59.4%	40.6 %
RCM Services Division	0.0%	0.0%	42.1%	0.8%	24.4%	67.3%	32.7 %
Consolidated	4.1%	0.9%	20.2%	9.0%	9.8%	44.0%	56.0 %
Three Months Ended December 31, 2013							
QSI Dental Division	2.8%	5.5%	21.2%	13.6%	4.0%	47.1%	52.9 %
NextGen Division	1.5%	1.2%	12.6%	10.5%	6.8%	32.6%	67.4 %
Hospital Solutions Division	2.5%	13.2%	144.2%	0.8%	35.4%	196.1%	(96.1)%
RCM Services Division	0.0%	0.0%	46.0%	0.6%	23.1%	69.7%	30.3 %
Consolidated	23.7%	1.4%	21.4%	8.9%	9.9%	65.3%	34.7 %

During the three months ended December 31, 2014, hardware and third party software constituted a slightly lower portion of cost of revenue compared to the same prior year period. The number of clients who purchase hardware and third party software and the dollar amount of hardware and third party software purchased fluctuates each quarter depending on the needs of our clients.

Our payroll and benefits expense associated with delivering our products and services decreased to 20.2% of consolidated revenue in the three months ended December 31, 2014 compared to 21.4% during the same period last year. The absolute level of consolidated payroll and benefit expenses increased from $23.3 million in the three months ended December 31, 2013 to $25.0 million in the three months ended December 31, 2014. The increase is primarily due to a $1.5 million increase in payroll and benefits expenses within the NextGen Division due to increased headcount and higher bonus expense, a $1.2 million increase within the RCM Services Division, as RCM is a service business which inherently has higher payroll costs as a percentage of revenue, a $0.1 million increase within the QSI Dental Division, partially offset by a $1.1 million decrease within the Hospital Solutions Division due to lower headcount. The amount of share-based compensation expense included in cost of revenue was not significant for the three months ended December 31, 2014 and 2013.

Cost of software revenue decreased to 4.1% of total revenue during the three months ended December 31, 2014 as compared to 23.7% for the same period a year ago mainly as a result of the $20.1 million Hospital impairment charge recorded in the prior year period.

As a result of the foregoing events and activities, our gross profit percentage increased to 56.0% for the three months ended December 31, 2014 versus 34.7% for the same prior year period.

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the three months ended December 31, 2014 increased 12.5% to $41.5 million as compared to $36.9 million for the prior year period. The increase in selling, general and administrative expenses consists primarily of:

- $2.5 million net increase in salaries and benefits due to increased headcount and higher bonus expense;
- $1.9 million increase in bad debt expense because the prior year period included a significant reduction to bad debt expense related to aggressive working capital management;
- $0.9 million increase in legal expenses due mostly to increased costs for shareholder litigation defense; and
- $0.6 million increase in acquisition related costs due mostly to post-acquisition fair value adjustments to contingent consideration related to Mirth; partially offset by
- $1.3 million net decrease in other selling and administrative expenses.

Share-based compensation expense was approximately $0.8 million and $0.5 million for the three months ended December 31, 2014 and 2013, respectively, and is included in the aforementioned amounts. Selling, general and administrative expenses as a percentage of revenue decreased from 33.9% in the three months ended December 31, 2013 to 33.6% in the three months ended December 31, 2014.

Research and Development Costs. Research and development costs for the three months ended December 31, 2014 and 2013 were $18.5 million and $13.2 million, respectively. Research and development costs as a percentage of revenue increased to 15.0% in the three months ended December 31, 2014 from 12.1% for the prior year period. The increase in research and development expenses is primarily due to the reduction in the capitalization rate of software costs in the current period as well as the continued investment in enhancements to our specialty template development, preparation for ICD-10 requirements, new product development and other enhancements to our existing products. The decrease in software capitalization rate reflects a trend towards a more agile development approach that inherently shortens the time frame during which development costs may be capitalized.

Additions to capitalized software costs result in reductions to reported research and development costs. For the three months ended December 31, 2014 and 2013, our additions to capitalized software were $3.2 million and $3.6 million, respectively. The decrease in capitalized software is primarily due to the lower capitalization rates of software development costs mentioned above and the cessation of software development costs capitalization related to the Hospital Solutions Division's software products as a result of the prior year impairment charge. For the three months ended December 31, 2014 and 2013, total research and development expenditures including both amounts expensed and capitalized was $21.7 million and $16.8 million, respectively.

We intend to continue to invest heavily in research and development to enhance our software to meet the Meaningful Use definitions under the ARRA as well as further integrate both ambulatory and inpatient products and to develop a new integrated inpatient and outpatient, web-based software platform as well as continue to bring additional functionality and features to the medical community.

Share-based compensation expense included in research and development costs was not significant for the three months ended December 31, 2014 and 2013.

Amortization of Acquired Intangible Assets. Amortization included in operating expenses related to acquired intangible assets decreased to $0.9 million for the three months ended December 31, 2014 from $1.2 million from the prior year period.

Provision for (Benefit of) Income Taxes. The provision for (benefit of) income taxes for the three months ended December 31, 2014 and 2013 was $1.5 million and $(6.6) million, respectively. The effective tax rates were 17.9% and 34.4% for the three months ended December 31, 2014 and 2013, respectively. The effective rate for the three months ended December 31, 2014 decreased as compared to the same prior year period primarily due to favorable discrete items included in the current period related to the enactment of the federal research and development tax credit statute, which had expired on December 31, 2013 and on December 19, 2014 was retroactively extended through December 31, 2014. The non-deductible portion of the Hospital impairment charge in the prior year also resulted in an incremental decrease in the effective tax rate for the three months ended December 31, 2014.

Comparison of the Nine Months Ended December 31, 2014 and December 31, 2013

Net Income. Our net income for the nine months ended December 31, 2014 was $16.6 million, or $0.28 and $0.27 per share, on a basic and fully diluted basis, respectively. In comparison, we earned $10.5 million, or $0.18 and $0.17 per share, on a basic and fully diluted basis, respectively, for the nine months ended December 31, 2013. The change in net income for the nine months ended December 31, 2014 was primarily attributed to the following:

- the prior year period included a $26.0 million impairment charge related to our Hospital Solutions Division while the current period does not include any such impairment charge
- revenue and gross profit benefited from an increase of $35.2 million, or 13.3%, in consolidated recurring services revenue including maintenance, RCM, EDI, and other revenue. Other revenue benefited from a $12.8 million, or 69.7%, increase in subscription revenue. Gross profit related to recurring services revenue grew $35.2 million, or 13.3%, as a result of revenue growth.
- this was partially offset by a 4.3% decline in consolidated system sales revenue related to a number of factors, including higher adoption rates by large physician groups resulting in a lower number of new opportunities, the consolidation of physician offices by hospitals and other large enterprises thereby reducing the number of potential opportunities, and an extension of the deadline to adopt stage two meaningful use requirements. The decline in consolidated system sales was partially offset by the impact of fewer sales credits and a reduction in reserves for sales returns in the Hospital Solutions division, which contributed to an increase in software revenue of $5.1 million as compared to the prior year period
- a $24.8 million, or 16.9%, increase in total operating expenses compared to the same prior year period. This increase is primarily due to a 95.4% increase in research and development expenses in the current period primarily due to higher gross expenditures in conjunction with lower capitalization rates of software development costs.
- an increase of $1.4 million in the provision for income taxes, primarily a result of the increased net income.

Revenue. Revenue for the nine months ended December 31, 2014 increased 9.8% to $361.8 million from $329.5 million for the nine months ended December 31, 2013. NextGen Division revenue increased 10.7% to $276.9 million from $250.1 million in the nine months ended December 31, 2013, QSI Dental Division revenue decreased 11.6% to $13.4 million from $15.1 million, RCM Services Division revenue increased 13.0% to $58.2 million from $51.5 million, and Hospital Solutions Division revenue increased 5.0% to $13.3 million from $12.7 million in the same prior year period.

System Sales. Revenue from consolidated system sales for the nine months ended December 31, 2014 decreased 4.3% to $62.3 million from $65.1 million in the same prior year period.

The following table breaks down our reported system sales into software, hardware and third-party software, and implementation and training services components on a consolidated and divisional basis for the nine months ended December 31, 2014 and 2013 (in thousands):

	Software	Hardware and Third Party Software	Implementation and Training Services	Total System Sales
Nine Months Ended December 31, 2014				
QSI Dental Division	$ 441	$ 878	$ 679	$ 1,998
NextGen Division	38,667	3,044	14,483	56,194
Hospital Solutions Division	2,549	(572)	1,680	3,657
RCM Services Division	301	4	122	427
Consolidated	$ 41,958	$ 3,354	$ 16,964	$ 62,276
Nine Months Ended December 31, 2013				
QSI Dental Division	$ 1,641	$ 984	$ 990	$ 3,615
NextGen Division	41,275	3,514	13,780	58,569
Hospital Solutions Division	(2,530)	470	4,660	2,600
RCM Services Division	294	—	—	294
Consolidated	$ 40,680	$ 4,968	$ 19,430	$ 65,078

The decrease in system sales was driven primarily by lower sales of software, hardware, and third party software to both new and existing clients for the NextGen Division and QSI Dental Division. NextGen Division sales in this category decreased 4.1%, or $2.4 million, to $56.2 million during the nine months ended December 31, 2014 from $58.6 million during the same prior year period while the QSI Dental Division experienced a 44.7%, or $1.6 million, decrease in category revenue to $2.0 million in the nine months ended December 31, 2014 as compared to $3.6 million in the same prior year period.

NextGen Division software license revenue decreased 6.3% in the nine months ended December 31, 2014 versus the same period last year. The Division’s software revenue accounted for 68.8% of divisional system sales revenue during the nine months ended December 31, 2014 compared to 70.5% during the same period a year ago resulting from lower sales to both new and existing customers. Software license revenue continues to be an area of primary emphasis for the NextGen Division. Implementation and training revenue related to system sales at the NextGen Division increased 5.1% in the nine months ended December 31, 2014 compared to the same prior year period. The amount of implementation and training services revenue is dependent on several factors, including timing of client implementations, the availability of qualified staff and the mix of services being rendered.

Software license revenue for the QSI Dental Division decreased 73.1% in the nine months ended December 31, 2014 versus the same period last year because the division's current software solution, QDW, is being sold primarily as a SaaS solution for which revenue is recognized over an extended period of time as other services revenue rather than upfront as software revenue.

Total system sales for the Hospital Solutions Division increased 40.6%, or $1.1 million, to $3.7 million in the nine months ended December 31, 2014 as compared to $2.6 million in the same prior year period. The increase in divisional category revenue is primarily due to lower software sales credits and related reserves, resulting in a $5.1 million increase in Hospital Solutions software sales in the nine months ended December 31, 2014 versus the same period last year. Implementation and training revenue related to system sales at the Hospital Solutions Division decreased 63.9%, in the nine months ended December 31, 2014 as compared to the same prior year period due to the recent decline in new software sales.

During the nine months ended December 31, 2014, 5.4% of consolidated system sales revenue was represented by hardware and third party software compared to 7.6% during the same period a year ago. The number of clients who purchase hardware and third party software and the dollar amount of hardware and third party software revenue fluctuates each quarter depending on the needs of clients. The inclusion of hardware and third party software in our sales arrangements is typically at the request of our clients.

Maintenance, EDI, RCM and Other Services. For the nine months ended December 31, 2014, our consolidated revenue from maintenance, EDI, RCM and other services grew 13.3% to $299.6 million from $264.4 million in the same prior year period. The increase is due to an increase across all categories of recurring service revenue.

The following table details maintenance, EDI, RCM and other services revenue by category on a consolidated and divisional basis for the nine months ended December 31, 2014 and 2013 (in thousands):

	Maintenance	EDI	RCM	Other	Total
Nine Months Ended December 31, 2014					
QSI Dental Division	$ 6,209	$ 3,723	$ —	$ 1,449	$ 11,381
NextGen Division	112,013	51,863	—	56,844	220,720
Hospital Solutions Division	7,332	94	—	2,235	9,661
RCM Services Division	431	596	54,517	2,255	57,799
Consolidated	$ 125,985	$ 56,276	$ 54,517	$ 62,783	$ 299,561
Nine Months Ended December 31, 2013					
QSI Dental Division	$ 6,275	$ 4,104	$ —	$ 1,143	$ 11,522
NextGen Division	104,264	45,591	—	41,693	191,548
Hospital Solutions Division	7,634	112	—	2,337	10,083
RCM Services Division	511	67	47,660	2,995	51,233
Consolidated	$ 118,684	$ 49,874	$ 47,660	$ 48,168	$ 264,386

Total category revenue for the NextGen Division for the nine months ended December 31, 2014 increased by 15.2% to $220.7 million from $191.5 million for the same prior year period. NextGen Division maintenance revenue for the three months ended December 31, 2014 grew 7.4% to $112.0 million from $104.3 million for the same prior year period primarily as a result of net additional licenses from both new and existing clients and the addition of maintenance revenue from Mirth, which was acquired on September 9, 2013. NextGen Division EDI revenue grew 13.8% to $51.9 million compared to $45.6 million in the same prior year period. The growth in NextGen EDI revenue has come from new clients and from further penetration of the division's existing client base. Other services revenue for the NextGen Division, which consists primarily of third party annual software license renewals, consulting services, SaaS fees, hosting services, and other subscriptions, increased 36.3% to $56.8 million in the nine months ended December 31, 2014 from $41.7 million in the same prior year period. Other services revenue benefited significantly from a $12.4 million increase in customer subscriptions, including Mirth subscriptions.

For the nine months ended December 31, 2014, RCM revenue for the RCM Services Division grew $6.9 million, or 14.4%, to $54.5 million compared to $47.7 million in the same prior year period. The growth in RCM revenue is primarily attributable to organic growth achieved through cross selling RCM services to existing NextGen Division clients, as well as the addition of new clients. For the Hospital Solutions Division, maintenance, EDI and other services revenue for the nine months ended December 31, 2014 decreased 4.2% as compared to the same prior year period primarily due to a decrease in maintenance revenue resulting from a decline in the amount of maintenance services provided to existing customers, partially offset by a decline in sales returns related to maintenance revenue. QSI Dental Division maintenance, EDI and other services revenue for the nine months ended December 31, 2014 and 2013 remained fairly consistent at $11.4 million and $11.5 million, respectively.

Cost of Revenue. Cost of revenue for the nine months ended December 31, 2014 increased 0.3% to $167.3 million from $166.8 million in the same prior year period and the cost of revenue as a percentage of revenue decreased to 46.2% from 50.6%. The decrease in cost of revenue as a percentage of revenue is primarily due to the $20.1 million Hospital impairment charge recorded to cost of software revenue in the prior year period, which is partially offset by an increase in cost of revenue related to a change in the mix of revenues toward recurring services revenue, which have historically experienced a lower profit margin than system sales. For the nine months ended December 31, 2014, recurring services revenue comprised 82.8% of consolidated revenue, as compared to 80.2% in the prior year period.

The following table details revenue and cost of revenue on a consolidated and divisional basis for the nine months ended December 31, 2014 and 2013 (in thousands):

	Nine Months Ended December 31,			
	2014	%	2013	%
QSI Dental Division				
Revenue	$ 13,379	100.0%	$ 15,137	100.0 %
Cost of revenue	6,818	51.0%	6,924	45.7 %
Gross profit	$ 6,561	49.0%	$ 8,213	54.3 %
NextGen Division				
Revenue	$ 276,914	100.0%	$ 250,117	100.0 %
Cost of revenue	95,459	34.5%	81,082	32.4 %
Gross profit	$ 181,455	65.5%	$ 169,035	67.6 %
Hospital Solutions Division				
Revenue	$ 13,318	100.0%	$ 12,683	100.0 %
Cost of revenue	10,723	80.5%	12,713	100.2 %
Gross profit (loss)	$ 2,595	19.5%	$ (30)	(0.2)%
RCM Services Division				
Revenue	$ 58,226	100.0%	$ 51,527	100.0 %
Cost of revenue	41,633	71.5%	35,422	68.7 %
Gross profit	$ 16,593	28.5%	$ 16,105	31.3 %
Unallocated cost of revenue	$ 12,690	N/A	$ 30,668	N/A
Consolidated				
Revenue	$ 361,837	100.0%	$ 329,464	100.0 %
Cost of revenue	167,323	46.2%	166,809	50.6 %
Gross profit	$ 194,514	53.8%	$ 162,655	49.4 %

Gross profit margins for the QSI Dental Division and NextGen Division decreased for the nine months ended December 31, 2014 compared to the same prior year period primarily due to decreases in total divisional system sales. Gross profit margin for the RCM Services Division decreased primarily as a result of higher salaries and benefits included in cost of revenue for the nine months ended December 31, 2014 as compared to the same prior year period. The gross profit (loss) margin for the Hospital Solutions Division in the nine months ended December 31, 2014 benefited from an increase in high-margin software sales resulting from lower returns and related reserves in the current period, combined with a decline in cost of revenue due to lower payroll and related benefits costs and the cessation of capitalized software cost amortization subsequent to the Hospital impairment. The decrease in unallocated cost of revenue is primarily due to the $20.1 million Hospital impairment charge recorded in the prior year period.

The following table details the individual components of cost of revenue and gross profit (loss) as a percentage of total revenue on a consolidated and divisional basis for the nine months ended December 31, 2014 and 2013:

	Software	Hardware and Third Party Software	Payroll and Related Benefits	EDI	Other	Total Cost of Revenue	Gross Profit (Loss)
Nine Months Ended December 31, 2014							
QSI Dental Division	0.0%	4.8%	30.3%	7.9%	8.0%	51.0%	49.0 %
NextGen Division	1.3%	0.8%	12.6%	11.5%	8.3%	34.5%	65.5 %
Hospital Solutions Division	0.0%	0.1%	64.4%	0.4%	15.6%	80.5%	19.5 %
RCM Services Division	0.0%	0.0%	46.4%	0.9%	24.2%	71.5%	28.5 %
Consolidated	4.5%	0.8%	20.6%	9.2%	11.1%	46.2%	53.8 %
Nine Months Ended December 31, 2013							
QSI Dental Division	2.7%	4.9%	20.8%	13.5%	3.8%	45.7%	54.3 %
NextGen Division	0.5%	1.3%	12.4%	11.0%	7.2%	32.4%	67.6 %
Hospital Solutions Division	2.9%	3.6%	68.5%	0.5%	24.7%	100.2%	(0.2)%
RCM Services Division	0.0%	0.0%	44.7%	0.7%	23.3%	68.7%	31.3 %
Consolidated	9.9%	1.3%	20.0%	9.1%	10.3%	50.6%	49.4 %

During the nine months ended December 31, 2014, hardware and third party software constituted a lower portion of cost of revenue compared to the same prior year period. The number of clients who purchase hardware and third-party software and the dollar amount of hardware and third-party software purchased fluctuates each quarter depending on the needs of our clients.

Gross margin for the Hospital Solutions Division increased to 19.5% for the nine months ended December 31, 2014 as compared to (0.2)% for the same prior year period. This is primarily a result of an increase in high-margin software sales resulting from lower returns and related reserves in the current period.

Our payroll and benefits expense associated with delivering our products and services increased slightly to 20.6% of consolidated revenue in the nine months ended December 31, 2014 compared to 20.0% during the same period last year. The absolute level of consolidated payroll and benefit expenses grew from $65.8 million in the nine months ended December 31, 2013 to $74.6 million in the nine months ended December 31, 2014. The increase is primarily due to a $4.1 million increase in payroll and benefits expenses within the NextGen Division, resulting from increased headcount compared to the prior year period, partially due to the inclusion of Mirth, a $4.0 million increase within the RCM Services Division, as RCM is a service business which inherently has higher payroll costs as a percentage of revenue, a $0.9 million increase within the QSI Dental Division, and a $0.1 million decrease within the Hospital Solutions Division. The amount of share-based compensation expense included in cost of revenue was not significant for nine months ended December 31, 2014 and 2013.

Other cost of revenue, which primarily consists of third party annual licenses, hosting costs and outsourcing costs, increased to 11.1% of total revenue during the nine months ended December 31, 2014 as compared to 10.3% for the same period a year ago. The increase is due to a change in mix of other services revenue sold as compared to the prior year period.

Cost of software revenue decreased to 4.5% of total revenue during the nine months ended December 31, 2014 as compared to 9.9% for the same period a year ago mainly as a result of the $20.1 million Hospital impairment charge recorded in the prior year period

As a result of the foregoing events and activities, our gross profit percentage increased to 53.8% for the nine months ended December 31, 2014 versus 49.4% for the same prior year period.

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the nine months ended December 31, 2014 increased 5.7% to $116.9 million as compared to $110.5 million for the prior year period. The increase in these expenses is partially due to the inclusion of expenses for Mirth, acquired on September 9, 2013, in the results for the nine months ended December 31, 2014. The increase in selling, general and administrative expenses, including the impact of Mirth, consists primarily of:

- $7.8 million net increase in salaries and benefits due to increased headcount and higher bonus expense;
- $1.9 million increase in acquisition costs due mostly to post-acquisition fair value adjustments to contingent consideration related to Mirth; and
- $1.3 million increase in advertising costs as a result of our increased focus on heightened brand awareness plus added utilization of online advertising and media placement; partially offset by
- $1.6 million decrease in sales commission due to a decline in new system sales;
- $2.8 million decrease in bad debt expense as a result of improved collections from greater emphasis on working capital management; and
- $0.2 million net decrease in other selling and administrative expenses.

Share-based compensation expense was approximately $2.1 million and $1.3 million for the nine months ended December 31, 2014 and 2013, respectively, and is included in the aforementioned amounts. Selling, general and administrative expenses as a percentage of revenue decreased from 33.6% in the nine months ended December 31, 2013 to 32.3% in the nine months ended December 31, 2014.

Research and Development Costs. Research and development costs for the nine months ended December 31, 2014 and 2013 were $51.6 million and $26.4 million, respectively. Research and development costs as a percentage of revenue increased to 14.3% in the nine months ended December 31, 2014 from 8.0% for the prior year period. The increase in research and development expenses is primarily due to the reduction in the capitalization rate of software costs in the current period, the acquisition of Mirth, as well as the continued investment in enhancements to our specialty template development, preparation for ICD-10 requirements, new product development and other enhancements to our existing products. The decrease in software capitalization rate reflects a trend towards a more agile development approach that inherently shortens the time frame during which development costs may be capitalized.

Additions to capitalized software costs result in reductions to reported research and development costs. For the nine months ended December 31, 2014 and 2013, our additions to capitalized software were $9.5 million and $18.9 million, respectively. The decrease in capitalized software is primarily due to the lower capitalization rates of software development costs mentioned above and the cessation of software development costs capitalization related to the Hospital Solutions Division's software products as a result of the prior year impairment charge. For the nine months ended December 31, 2014 and 2013, total research and development expenditures including both amounts expensed and capitalized was $61.1 million and $45.3 million, respectively.

Share-based compensation expense included in research and development costs was not significant for the nine months ended December 31, 2014 and 2013.

Amortization of Acquired Intangible Assets. Amortization included in operating expenses related to acquired intangible assets decreased to $2.8 million for the nine months ended December 31, 2014 from $3.7 million in the same prior year period due mostly to the cessation of amortization of acquired intangible assets related to the Hospital Solutions Division as a result of the prior year impairment charge.

Provision for Income Taxes. The provision for income taxes for the nine months ended December 31, 2014 and 2013 was $6.7 million and $5.2 million, respectively. The effective tax rate was 28.6% and 33.4% for the nine months ended December 31, 2014 and 2013, respectively. The effective rate for the nine months ended December 31, 2014 decreased as compared to the same prior year period primarily due to an increase in benefit from the federal research and development tax credit partially offset by a decrease in benefit from the qualified production activities deduction. The federal research and development tax credit statute, which had expired on December 31, 2013, was retroactively extended through December 31, 2014 on December 19, 2014. The non-deductible portion of the Hospital impairment charge in the prior year also resulted in an incremental decrease in the effective tax rate for the nine months ended December 31, 2014.

Liquidity and Capital Resources

The following table presents selected financial statistics and information for the nine months ended December 31, 2014 and 2013 (in thousands):

	Nine Months Ended December 31,	
	2014	2013
Cash and cash equivalents and marketable securities	$ 124,822	$ 93,989
Net increase (decrease) in cash and cash equivalents and marketable securities	$ 11,021	$ (24,022)
Net income	$ 16,589	$ 10,479
Net cash provided by operating activities	$ 58,706	$ 71,571
Number of days of sales outstanding (1)	78	106

(1) Days sales outstanding is equal to accounts receivable divided by average daily revenue.

Cash Flows from Operating Activities

Cash provided by operations has historically been our primary source of cash and has primarily been driven by our net income.

The following table summarizes our consolidated statements of cash flows for the nine months ended December 31, 2014 and 2013 (in thousands):

	Nine Months Ended December 31,	
	2014	2013
Net income	$ 16,589	$ 10,479
Non-cash expenses	26,577	52,634
Cash from net income (as adjusted)	43,166	63,113
Change in accounts receivable	8,779	23,451
Change in other assets and liabilities	6,761	(14,993)
Net cash provided by operating activities	$ 58,706	$ 71,571

Net cash provided by operating activities for the nine months ended December 31, 2014 and 2013 was approximately $58.7 million and $71.6 million, respectively. Net income increased by $6.1 million for the nine months ended December 31, 2014 and non-cash expenses decreased by $26.0 million primarily due to the $26.0 million Hospital impairment charge recorded in the prior year period. A decline of $14.7 million in cash flows is attributable to the substantial reduction in accounts receivable in the same prior year period due to aggressive working capital management; offset by higher cash flows from changes in other assets and liabilities of $21.8 million, which mostly relates to changes in income taxes receivable, accounts payable, other liabilities and deferred revenue.

The Company continues to place strong emphasis on working capital management and collections as reflected by a reduction of days sales outstanding (“DSO”) in comparison to the prior year period. Specifically, during the nine months ended December 31, 2014, DSO decreased by 9 days to 78 days. In comparison, DSO decreased by 16 days to 106 days during the same prior year period. Based on our results for the nine months ended December 31, 2014, we anticipate being able to continue generating sufficient cash from operations for the remainder of fiscal year 2015.

Cash Flows from Investing Activities

Net cash used in investing activities for the nine months ended December 31, 2014 and 2013 was approximately $15.6 million and $62.5 million, respectively. The $46.9 million decrease in net cash used in investing activities is primarily due to $35.0 million of cash paid for the acquisition of Mirth in the prior year period, a $9.4 million decrease in additions to capitalized software costs, a $3.1 million decrease in purchases of marketable securities, partially offset by a $2.6 million decrease in proceeds from the sales and maturities of marketable securities.

Cash Flows from Financing Activities

Net cash used in financing activities for the nine months ended December 31, 2014 and 2013 was $32.6 million and $33.0 million, respectively. During the nine months ended December 31, 2014, we paid $32.1 million in dividends to shareholders and $0.7 million in contingent consideration related to acquisitions, which was partially offset by proceeds of $0.2 million from the issuance of shares under the employee share purchase plan. In comparison, during the same prior year period, we paid $31.5 million in dividends to shareholders and $3.7 million in contingent consideration related to acquisitions, which was partially offset by proceeds of $2.2 million from the exercise of stock options.

Cash and Cash Equivalents and Marketable Securities

At December 31, 2014, we had combined cash and cash equivalents and marketable securities of $124.8 million, reflecting an increase of $11.0 million from the comparable balance as of March 31, 2014. This increase principally reflects the contribution to cash from net income and the continued decrease in DSO from an emphasis on working capital management in the current year.

We may use a portion of these funds towards future acquisitions, although the timing and amount of funds to be used has not been determined. We intend to expend some of these funds for the development of products complementary to our existing product line as well as new versions of certain of our products. These developments are intended to take advantage of more powerful technologies and to increase the integration of our products. Such expenditures will be funded from cash on hand and cash flows from operations.

Our investment policy is determined by our Board of Directors. We currently maintain our cash in very liquid short term assets including tax exempt and taxable money market funds, Certificates of Deposit and short term Municipal Bonds with average maturities of 365 days or less at the time of purchase. Our Board of Directors continues to review alternate uses for our cash including, but not limited to, payment of a special dividend, initiation of a stock buyback program, an expansion of our investment policy and other items. Additionally, it is possible that we will utilize some or all of our cash to fund acquisitions or other similar business activities. Any or all of these programs could significantly impact our investment income in future periods.

In January 2007, our Board of Directors adopted a practice whereby we intend to pay a regular quarterly dividend on our outstanding common stock, subject to further review and approval, sufficiency of funds and the establishment of record and distribution dates by our Board of Directors prior to the declaration of each such quarterly dividend. We anticipate that future quarterly dividends, if and when declared by our Board of Directors pursuant to this practice, would likely be distributable on or about the fifth day of each January, April, July and October. The Board of Directors has historically shown a strong commitment to the payment of a regular dividend and will continue to evaluate the continued payment of dividends based on our operating cash flows and future capital requirements.

On January 21, 2015, the Board of Directors approved a quarterly cash dividend of $0.175 per share on our outstanding shares of common stock, payable to shareholders of record as of March 13, 2015 with an expected distribution date on or about April 3, 2015.

Our Board of Directors declared the following dividends during the periods presented:

Declaration Date	Record Date	Payment Date	Per Share Dividend	
May 28, 2014	June 13, 2014	July 3, 2014	$	0.175
July 23, 2014	September 12, 2014	October 3, 2014		0.175
October 22, 2014	December 12, 2014	January 2, 2015		0.175
Fiscal year 2015			$	0.525
May 22, 2013	June 14, 2013	July 5, 2013	$	0.175
July 24, 2013	September 13, 2013	October 4, 2013		0.175
October 23, 2013	December 13, 2013	January 3, 2014		0.175
January 22, 2014	March 14, 2014	April 4, 2014		0.175
Fiscal year 2014			$	0.70

Management believes that its cash, cash equivalents and marketable securities on hand at December 31, 2014, together with its cash flows from operations, will be sufficient to meet its working capital and capital expenditure requirements, as well as any dividends to be paid in the ordinary course of business, for the next twelve months. Our Board of Directors will continue to evaluate the strategic use of our cash towards payment of dividends in light of both working capital and capital expenditure requirements.

Contractual Obligations

The following table summarizes our significant contractual obligations at December 31, 2014 and the effect that such obligations are expected to have on our liquidity and cash in future periods:

		For the year ended March 31,					
Contractual Obligations	Total	2015 (remaining three months)	2016	2017	2018	2019	2020 and beyond
Operating lease obligations	$ 43,944	$ 2,040	$ 7,324	$ 7,069	$ 7,082	$ 4,034	$ 16,395
Contingent consideration and other acquisition related liabilities (excluding share-based payments)	$ 625		$ 313	$ 312	—	—	—
Total	$ 44,569	$ 2,040	$ 7,637	$ 7,381	$ 7,082	$ 4,034	$ 16,395

The deferred compensation liability as of December 31, 2014 was $5,477, which is not included in the table above as the timing of future benefit payments to employees is not determinable.

The uncertain tax position liability as of December 31, 2014 was $777, which is not included in the table above as the timing of expected payments is not determinable.

In addition, future minimum lease payments of approximately $6.2 million relating to the lease amendment of our St. Louis location, subsequently executed in January 2015, are not reflected in the table above.

Recent Accounting Pronouncements

Refer to Note 1, "Summary of Significant Accounting Policies," of our notes to consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q for a discussion of new accounting standards.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

There is little to no market risk as we currently maintain our cash in very liquid short term assets including tax exempt and taxable money market funds and short-term U.S. Treasury securities with maturities of 90 days or less at the time of purchase.

Although we have international operations, the impact of foreign currency fluctuations have not been material to our financial position or operating results.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively) have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Security Exchange Act of 1934, as amended, the "Exchange Act") as of December 31, 2014, the end of the period covered by this Quarterly Report on Form 10-Q (the “Evaluation Date”). They have concluded that, as of the Evaluation Date, these disclosure controls and procedures were effective to ensure that material information relating to the Company and its consolidated subsidiaries would be made known to them by others within those entities and would be disclosed on a timely basis. The Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are designed, and are effective, to give reasonable assurance that the information required to be disclosed by us in reports that we file under the Exchange Act is recorded, processed, summarized and reported within the time period specified in the rules and forms of the SEC. They have also concluded that the our disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that are filed or submitted under the Exchange Act are accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

During the quarter ended December 31, 2014, there were no changes in our “internal control over financial reporting” (as defined in Rule 13a-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management, including our Chief Executive Officer and Chief Financial Officer, has concluded that our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance of achieving their objectives and are effective at that reasonable assurance level. However, management can provide no assurance that our disclosure controls and procedures or our internal control over financial reporting can prevent all errors and all fraud under all circumstances. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been or will be detected. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Hussein Litigation

On October 7, 2013, a complaint was filed against the Company and certain of the Company’s officers and directors in the Superior Court of the State of California for the County of Orange, captioned Ahmed D. Hussein v. Sheldon Razin, Steven Plochocki, Quality Systems, Inc. and Does 1-10, inclusive, No. 30-2013-00679600-CU-NP-CJC, by Ahmed Hussein, a former director and significant shareholder of the Company. The Company filed a demurrer to the complaint, which the court granted on April 10, 2014. An amended complaint was filed on April 25, 2014. The amended complaint generally alleges fraud and deceit, constructive fraud, negligent misrepresentation and breach of fiduciary duty in connection with statements made to the Company’s shareholders regarding the Company’s financial condition and projected future performance. The amended complaint seeks actual damages, exemplary and punitive damages and costs. The Company filed a demurrer to the amended complaint. On July 29, 2014, the court sustained the demurrer with respect to the breach of fiduciary duty claim, and overruled the demurrer with respect to the fraud and deceit claims. On August 28, 2014, the Company filed an answer and cross complaint.

Federal Securities Class Action

On November 19, 2013, a putative class action complaint was filed on behalf of the shareholders of the Company other than the defendants against the Company and certain of the Company’s officers and directors in the United States District Court for the Central District of California, by a shareholder of the Company. After the court appointed lead plaintiffs and lead counsel for this action, and recaptioned the action *In re Quality Systems, Inc. Securities Litigation*, No. 8L13-cv-01818-CJC(JPRx), lead plaintiffs filed an amended complaint on April 7, 2014. The amended complaint, which is substantially similar to the litigation described above under the caption "Hussein Litigation," generally alleges that statements made to the Company’s shareholders regarding the Company’s financial condition and projected future performance were false and misleading in violation of Section 10(b) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and that the individual defendants are liable for such statements because they are controlling persons under Section 20(a) of the Exchange Act. The complaint seeks compensatory damages, court costs and attorneys' fees. The Company filed a motion to dismiss the amended complaint on June 20, 2014, which the court granted on October 20, 2014, dismissing the complaint with prejudice. Plaintiffs filed a motion for reconsideration of the Court's order, which the Court denied on January 5, 2015.

Shareholder Derivative Litigation

On January 24, 2014, a complaint was filed against the Company and certain of the Company’s officers and current and former directors in the United States District Court for the Central District of California, captioned Timothy J. Foss, derivatively on behalf of himself and all others similarly situated, vs. Craig A. Barbarosh, George H. Bristol, James C. Malone, Peter M. Neupert, Morris Panner, D. Russell Pflueger, Steven T. Plochocki, Sheldon Razin, Lance E. Rosenzweig and Quality Systems, Inc., No. SACV14-00110-DOC-JPPx, by Timothy J. Foss, a shareholder of the Company. The complaint arises from the same allegations described above related to the “complaints filed by Mr. Hussein” and the Deerfield Beach Police Pension Fund and generally alleges breach of fiduciary duties, abuse of control and gross mismanagement by the Company’s directors, in addition to unjust enrichment and insider selling by individual directors. The complaint seeks compensatory damages, restitution and disgorgement of all profits, court costs, attorneys’ fees and implementation of enhanced corporate governance procedures. The parties have agreed to stay this litigation pending Plaintiffs' decision regarding possible appeal in the Federal Securities Class Action.

In addition to the above, we have experienced legal claims by customers regarding product and contract disputes and from time to time, claims by other third parties asserting that we have infringed their intellectual property rights. We believe that these claims, including those filed by Mr. Hussein, the Deerfield Beach Police Pension Fund and the shareholder derivative action, are without merit and intend to defend against them vigorously; however, we could incur substantial costs and diversion of management resources even if we are ultimately successful in the defense of such claims. Litigation is inherently uncertain and always difficult to predict. We refer you to the discussion of infringement and litigation risks in our “Item 1A. Risk Factors” section of our Annual Report.

ITEM 1A. RISK FACTORS

Our business is subject to many risks and uncertainties, which may materially and adversely affect our future business, prospects, financial condition and results of operations. These risk factors are disclosed in “Item 1A. Risk Factors” in our Annual Report.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit Number	Exhibit Description	Filed Herewith
31.1	Certification of Principal Executive Officer Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	X
31.2	Certification of Principal Financial Officer Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	X
32.1	Certification of 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.	X
101.INS**	XBRL Instance	
101.SCH**	XBRL Taxonomy Extension Schema	
101.CAL**	XBRL Taxonomy Extension Calculation	
101.LAB**	XBRL Taxonomy Extension Label	
101.PRE**	XBRL Taxonomy Extension Presentation	

** XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of section 11 or 12 of the Securities and Exchange Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise is not subject to liability under these section.

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.

			QUALITY SYSTEMS, INC.
Date:	January 22, 2015	By:	/s/ Steven T. Plochocki
			Steven T. Plochocki
			Chief Executive Officer (Principal Executive Officer)
Date:	January 22, 2015	By:	/s/ Paul A. Holt
			Paul A. Holt
			Chief Financial Officer (Principal Accounting Officer)

EXHIBIT 31.1

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER REQUIRED BY
RULE 13A-14(A) OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Steven T. Plochocki, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Quality Systems, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: January 22, 2015

By: /s/ Steven T. Plochocki
Steven T. Plochocki
Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER REQUIRED BY RULE 13A-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Paul A. Holt, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Quality Systems, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: January 22, 2015

By: /s/ Paul A. Holt
Paul A. Holt
Chief Financial Officer
(Principal Accounting Officer)

EXHIBIT 32.1

CERTIFICATION OF 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

In connection with the Quarterly Report on Form 10-Q of Quality Systems, Inc. (the “Company”) for the quarterly period ended December 31, 2014 (the “Report”), the undersigned hereby certify in their capacities as Chief Executive Officer and Chief Financial Officer of the Company, respectively, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date:	January 22, 2015	By:	/s/ Steven T. Plochocki
			Steven T. Plochocki
			Chief Executive Officer (Principal Executive Officer)
Date:	January 22, 2015	By:	/s/ Paul A. Holt
			Paul A. Holt
			Chief Financial Officer (Principal Accounting Officer)

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signatures that appear in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.