Presentation

Operator

Welcome to Teladoc's First Quarter 2017 Earnings Conference Call and Webcast. [Operator Instructions]

It is now my pleasure to turn the floor over to Ms. Jisoo Suh, Director of Investor Relations. You may begin.

Jisoo Suh
Director of Investor Relations

Thank you, operator, and good afternoon, everyone. We look forward to discussing our first quarter 2017 results with you today. Joining me for Teladoc's conference call are Jason Gorevic, our President and Chief Executive Officer; Mark Hirschhorn, our Chief Operating Officer and Chief Financial Officer; and Adam Vandervoort, our Chief Legal Officer and Corporate Secretary.

Today, after the market closed, we issued a press release announcing our first quarter 2017 results and filed Form 10-Q. The release and filing are available in the Investors Relations section of teladoc.com. As a reminder, Teladoc intends to avail itself of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Certain statements made during this call will be forward-looking statements within the meaning of that law. These forward-looking statements are subject to risks, uncertainties and other factors that could cause Teladoc's actual results to differ materially from those expressed or implied by the forward-looking statements. For additional information on the risks facing Teladoc, please refer to our filings with the SEC.

We'll start today's call with brief prepared remarks followed by Q&A. Today's call will also contain certain non-GAAP financial measures, which we believe are important in evaluating our performance. For more details on these measures, the most comparable GAAP measures and a reconciliation of the 2, please refer to the press release posted on teladoc.com.

I will now turn the call over to Jason.

Jason Gorevic
Chief Executive Officer, President and Director

Thanks, Jisoo, and good afternoon, everyone. I'm excited to report that we carried strong momentum and excellent results into the first quarter of 2017. Teladoc continues to demonstrate consistently solid execution and benefit from the overall network effects surrounding our business and the virtual care industry in general.

In the first quarter, we met or exceeded our guidance across each of our key metrics, in which we recorded total revenue of around $43 million or a growth of approximately 60%, adjusted EBITDA loss of $9 million, which improved from approximately $12 million in the same period last year. Membership of 20.1 million lives or a growth of 34% over prior year and over 2.6 million newly added lives since year-end. And finally, visits of approximately 385,000 or growth of 60%. This represents a quarterly annualized utilization rate of approximately 7.6% or 127 basis point increase year-over-year, reflecting the high impact of our member engagement strategies combined with a relatively short but severe cold and flu season in January and February.

As I noted, Teladoc's record-high utilization rates reflect our surround-sound engagement strategy, deployed via traditional channels such as direct mail, including the delivery of new member welcome kits as well as via highly targeted and increasingly cost-efficient e-mail and digital campaigns.

Turning to an update on new client business, we observed seamless implementations during the first quarter from accounts such as Southern California Edison, Marriott Vacations Worldwide and Yale University, among many others as well as from health plan clients that we previously mentioned, including Fallon and AultCare that went live during the period.

Meanwhile, continued demand for our virtual care delivery solutions resulted in newly signed accounts such as Dillard's, Bayer and Paychex to name a few employer clients as well as Pacific Source in the health plan space. These clients are all expected to go live later this year.

Our behavioral health and dermatology products continue to resonate as existing clients like KPMG, Chesapeake Energy and Lowe's added to their core general medical specialties. We also have significant interest in our specialty products from our health plan partners and have begun to roll out behavioral health and dermatology into their large books of business.

I'd also like to highlight our continued success in the provider market where our solutions now support more than 140 hospitals across the nation. We are incredibly proud to announce newly signed agreements with MultiCare Health System comprising 7 hospitals in Washington; WellSpan Health System, comprising 6 hospitals in Central Pennsylvania; as well as recently expanded relationship with the Mount Sinai Health System in New York.

Our increasing client roster reflects the flexibility of solutions we offer to the hospital market as well as our compelling vision to help providers build healthier communities and improve patient outcomes. We are also pleased by contributions from our behavioral health offering, in which revenue more than doubled year-over-year to reach approximately $5 million in the first quarter. We expect to maintain this trend throughout 2017.

Before moving on, I'd like to take a moment to go over our previously announced appointment of Peter Nieves to the new role of EVP and Chief Revenue Officer reporting directly to me. It's always been a priority of mine and the board to stay ahead of our growth curve by putting the people and organizational structure in place to take us to the next level. Pete is an accomplished commercial leader with extensive capabilities that align perfectly with Teladoc's strategic vision. He has deep understanding of the employer, payer and broker consultant landscape and previously came from Optum, where he served as the Executive VP of Employer Solutions, leading all aspects of the employer market, sales and account management strategy. And before that, led global growth strategy for Mercer. He's already hit the ground running by working to further integrate our overall sales operations framework as we continue to scale, identifying ways to extend our leadership position, get greater leverage out of our sales and product development efforts across all client segments and deliver on our broader financial objectives.

Now I'd like to offer a few timely insights from Teladoc's second annual client summit held last week at our Lewisville headquarters. We hosted approximately 40 clients who are leaders in their respective industries, including 15 of the Fortune 1000 and together, comprised more than 700,000 of our members. We are encouraged by clients such as TD Ameritrade who have been using Teladoc for several years and are achieving consistent step function growth in utilization levels to reach over 20% on an annualized basis, incorporating Teladoc as the centerpiece of their total rewards program across their distributed workforce.

We also had the chance to discuss our product and capability road map as Teladoc continues to expand our service offerings to achieve our goal of providing a broad and integrated virtual care platform for our members and clients. Specifically, our clients reinforced our vision by expressing the following feedback and broad themes: First, a sincere interest in our newer specialty products, with particular excitement regarding the opportunity to address the massive problem of untreated mental illness to our behavioral health product; secondly, strong demand from -- for the continued expansion of our clinical offerings to broaden the scope of services available to members and to provide solutions that help our clients address more complex and costly medical conditions; third, an appreciation for our select integrations with other service providers who are important partners of our client health care management strategies. For example, we were highly praised for our recently announced partnership with Accolade. And finally, clients expressed eagerness in collaborating with us to find new, creative and targeted ways to engage their employees and drive higher utilization of the Teladoc platform.

Now I'd like to provide a quick update on the legal and regulatory front where we continue to be cautiously encouraged by current legislative developments in Texas. As many of you know, a bill that makes it clear that telehealth will continue uninterrupted in Texas has been making its way through the state legislature and could become law in the next few weeks. The passage of this bill into law would resolve our outstanding issues with the Texas Medical Board and would represent a significant victory for the people of Texas in securing their path to quality, affordable and accessible health care.

As you can see, we have a lot of exciting things going on right now Teladoc. I'm very pleased with the results we delivered in the first quarter, and I believe that we are on track to reach our year-end objectives where we continue to target the fourth quarter to achieve adjusted EBITDA breakeven. We continue to execute on our growth strategy of extending our industry leadership and success in cross-selling new and innovative solutions to existing members. Having just wrapped up our client summit, it's very evident that our clients and members realize and appreciate the value of our platform. Given the growing awareness and acceptance of telemedicine, I have never been more optimistic about the opportunity in front of us.

With that, I'll now turn over the call to Mark to review our first quarter results in greater detail.

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

Thanks, Jason, and good afternoon, everyone. Let's start with revenue where we recorded $42.9 million, representing 60% growth over the prior period. Organic revenue growth was approximately 41% over the same period last year. Subscription access fees accounted for $34.3 million or 80% of our total revenue and grew over 65% year-over-year, reflecting overall membership expansion and contributions from HealthiestYou. As a reminder, our core small but midsized employer client base is comprised of accounts principally sold through brokers who embraced bundled, visits-included contracts with higher PEPM rates. Subscription access fees grew 13% sequentially, reflecting growth in covered lives since year-end.

Our average per employee per month fee, or PEPM, across our business was $0.58 compared to $0.47 in the prior year period, reflecting the positive impact from the increased visits-included subscription mix I just noted. Visits revenue for the quarter were almost 40% year-over-year to $8.6 million, 100% of that growth is organic.

Turning to total visits, we completed approximately 385,000 visits in the quarter or growth at 60%. This equates to a quarterly annualized utilization rate of 7.6%, which is the highest we've ever recorded in the quarter and 127 basis point increase over the same period in 2016 and a 56 basis point increase from Q4 of 2016. Gross margin in the quarter was 72%, up slightly from 71% a year ago. The slight year-over-year increase is attributable to the company's revenue mix where subscription revenues accounted for 80% of our revenue in this quarter compared to 77% of our revenue in the prior year period.

Total operating expenses in the first quarter were $43 million, which increased 34% over the prior year primarily due to investments in marketing, sales and G&A in order to support our 60% revenue growth. We take an opportunistic approach to investing in our infrastructure. For example, our new Phoenix office was initially focused on sales and marketing. This past quarter, we completed the final stages of creating a secondary operation center by taking advantage of the space available to us. To be clear, this was not a capacity-driven build-out, rather, we saw tremendous value to our clients and members by ensuring that we have a fully redundant operations site, with disaster recovery options, to maintain continuity of service under all circumstances.

Operating expenses as a percentage of revenue declined year-over-year by over 1,900 basis points, with leveraging G&A, technology and development as well as legal expenses. Sequentially, operating expenses increased by approximately $5 million, with much of that increase in absolute dollar terms, attributable to member onboarding activities and additional advertising and marketing expenses. As we've stated in the past, the first calendar quarter is our heaviest period for marketing and advertising costs as our focus is engaging members from newly onboarded clients.

Our adjusted EBITDA improved to a loss of $9.1 million compared to a loss of $11.9 million in the same period last year. We continue to make progress on our goal of being adjusted EBITDA breakeven in the fourth quarter of this year. Net loss in the quarter was $15.7 million compared to $15.3 million in the same period last year. Net loss per share was $0.30 compared to a net loss of $0.40 in the same period last year, reflecting our higher share count in the current period. Our weighted average common shares outstanding were 52.2 million shares in this period compared to 38.6 million shares in the same period last year, reflecting the issuance of 7.9 million shares from our follow-on offering this past January and 7 million shares issued for our acquisition last July.

Turning to our balance sheet, we ended the quarter with over $175 million in cash and short-term investments, reflecting proceeds from our follow-on offering. Our debt balance remained constant at $42.4 million. As Jason mentioned, our priority is to grow Teladoc's ability to play across the continuum of virtual care services and deliver greater value to our members and clients. We believe our strength and capital position affords us tremendous flexibility to both invest organically in our businesses and opportunistically look outside the company for value-accretive assets to expand the benefits of our platform.

Now I would like to provide our outlook for the second quarter of 2017, in which we currently expect total revenue between $44 million and $45 million and EBITDA loss between $10.5 million and $11.5 million and adjusted EBITDA loss between $6 million and $7 million. Total membership of approximately 20.5 million to 21 million members, total visits between 290,000 and 310,000 visits, and a net loss per share based on 54.5 million weighted average shares outstanding is expected to range from $0.26 to $0.28.

For the full year 2017, we continue to expect total revenue between $180 million and $185 million, and EBITDA loss between $31 million and $34 million, adjusted EBITDA loss between $19.5 million and $22.5 million, in which we target to achieve adjusted EBITDA breakeven in the fourth quarter of this year.

Total membership of approximately 21.5 million members to 23 million members, total visits between 1.4 million and 1.45 million visits and a net loss per share based on 54.2 million weighted average shares outstanding is expected to range from $0.85 to $0.91.
And with that, operator, please open the call for questions.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Lisa Gill of JP Morgan.

Michael Roman Minchak
JP Morgan Chase & Co, Research Division

It's actually Mike Minchak in for Lisa this afternoon. So with regards to the selling season for next year, I was just wondering if you could talk a little bit about the level of demand from perspective clients relative prior year's and sort of how that looks across the various vertical segments and anything new the clients may be looking for, for next that you might be able to offer?

Jason Gorevic
Chief Executive Officer, President and Director

Sure. Thanks, Mike. So I would say still a little early to try to develop or articulate trends for this selling season into 2018. With that said, I would say for us, health plan activity has been strong. Large employer activity similar to previous years, small market, meaning the small and midsized significantly more activity. But just remind you that, that occurs over the course of the year. It's not just January 1-centric. The hospital market has been ramping up significantly and we continue to see more demand coming out of that segment. Our specialty products, as I mentioned when I was talking about our client summit, are getting a lot of attention across the spectrum from employers, especially on the large employer market and from health plans as well. The only other thing, I guess, I would say that's different this year is that we're seeing more activity with employers and health plans and hospitals systems who previously chose one of our competitors and are coming to us for our solution and our ability to drive utilization. That's happening significantly more this year than it's happened in the past.

Michael Roman Minchak
JP Morgan Chase & Co, Research Division

Got it. And I think the past, you've pointed to opportunities to add lives with existing customers. So for example at Aetna, I think you added a couple million lives there but just a fraction of their total covered lives. Can you talk about the progress you're seeing just broadly and expanding the number of lives within existing customers and with the incremental opportunity there could look like over time?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, we've continued to see that trend where we -- especially in the health plan market, we sort of land and expand. That doesn't recur in the employer space but I would say, at UnitedAg, Blue Shield California, Premera are all good examples of where we are successfully doing that.

Operator

Your next question comes from Sean Weiland of Piper Jaffray.

Sean William Wieland
Piper Jaffray Companies, Research Division

So on the lift in utilization, can you maybe break that down a little bit in terms of which areas or markets did you see the most lift? Did you see any kind of cause and effect of something that you tried, maybe new in the quarter that either worked or didn't work regarding utilization?

Jason Gorevic
Chief Executive Officer, President and Director

Yes. Thanks, Sean. I would say our utilization lift occurred across our various market segments, probably you see the impact from the employers segment and the health plan segment more than you would from the provider segment. But what I would say, to answer the second part of your question, is that we have continued to refine our digital marketing efforts and especially our ability to do highly targeted digital marketing and that has yielded very strong results for us. We've -- I would say if you look at this first quarter of '17 versus first quarter of '16, it's substantially more targeted digital this year than there was a year ago.

Sean William Wieland
Piper Jaffray Companies, Research Division

And that delivers the greatest lift, do you think?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, there's no question. I mean we -- what we see always is when we layer on targeted digital with direct mail, with our onboarding welcome kits, we get both reach and frequency and being able to do the digital in a very targeted manner enables us to do it cost-effectively.

Sean William Wieland
Piper Jaffray Companies, Research Division

All right. And then to slide a follow-up in here, member onboarding cost, you said about $5 million of the sequential increase was due to member onboarding cost. What -- since this was a period where you probably added more members than in any other period, maybe takeaways from the quarter and ideas on how you can lower those member onboarding costs without impacting utilization, what's the thought process there?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

Sean, it's Mark. In fact, we noted that the $5 million came about as a result of both increased advertising as well as member onboarding costs. So you should think of that amount, about half that amount attributable to direct onboarding costs. As Jason noted, and to add to what he said regarding utilization, utilization for us really peaks in the fourth quarter, the last 3 years our utilization has peaked in the fourth quarter in each of those respective years and the amounts that we invest in onboarding, clearly is tied to the initial onboarding but coming into the end of the year, we've got obviously other campaigns that we may launch where we always end up seeing the impact in utilization. So it's far less of a question of bringing down those onboarding cost today and much more focused on the actual throughput of those investments. We're looking at the initiatives that drive the highest utilization. So we have a number of initiatives that we would focus on for certain employers and health plans and others that, again, still being sensitive to the costs, we realize, will have a greater impact on throttling up utilization.

Operator

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

James Auh
Cowen and Company, LLC, Research Division

This is James Auh on for Charles. So my question is can you give a percent of what percentage of your customer base subscribes more than one product offering? And also, has the level of your cross-selling activity been in line with expectations? And how much cross-selling is embedded in guidance?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

Yes, with regard to the number of members that are actively now receiving more than their initial service, we're right below 5%. So the penetration today is, I believe, on target with what we expected at the beginning of the year, but we expect many additional clients to take on those ancillary offerings throughout 2017. With respect to our ramp, I think Jason had noted earlier, we hosted over a dozen clients in our Lewisville facility this past week and in our annual client summit. The overwhelming feedback was that there was significant interest in behavioral and other products that we've recently launched. So we'd expect to see a lot of in-year revenue as well as extension of contracts to provide for those additional services throughout this year.

Jason Gorevic
Chief Executive Officer, President and Director

And I think, James, I would just add, that the health plan segment, for the first time, is showing significant interest in implementing those additional specialty products. So materially, all of the early adopters of those products were employers and now we're starting to see significant uptake from the health plans as well.

James Auh
Cowen and Company, LLC, Research Division

Okay, great. Also, for the quarter, you beat 1Q guidance. 2Q guidance looks pretty good. Can you speak to what you expect in the back half? Was something pulled forward and that's why you've reaffirmed full year guidance? Or is it just kind of a measure of conservatism?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

It's really measure of our comfort in our -- in the traction that we received at the beginning of the year and our ability to now to be very comfortable with our revenue ramp and of course, the lowering of the EBITDA loss quarter-over-quarter. We're very comfortable with what we've seen in the first -- really in the first 4 months of the year and we continue to march towards that Q4 objectives.

Operator

Your next question comes from the line of Andy Draper of SunTrust.

Alexander Yearley Draper
SunTrust Robinson Humphrey, Inc., Research Division

First question, could you maybe just sort of walk me through or help me understand, as the health systems are coming on, not maybe like, I think it was Yale you mentioned, Jason, it sounds like there's an actual customer for their employees but a health system partner, have you guys sort of finalized what that revenue model looks like and how -- who's paying? Or is that still an evolutionary process?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, so just -- Sandy, thanks for the question about the health systems. Just to clarify, Yale University is actually for the employees of Yale University, not Yale as the medical system. However, when we talk about others, we are, in fact, talking about the hospitals themselves. Now sometimes they're using them for their own employees, but when we talk about our hospital clients, for the most part, we're talking about them licensing our platform. It's a platform as a service model. We have a license fee, a base license fee and then there's a transaction fee as well. It differs depending on whether they're using our physicians in the Teladoc network or their own physicians, but there's a transaction fee regardless. Obviously, if they're using ours, then it's a significantly higher transaction fee. And from our perspective, we get great feedback from the hospital systems, and one of the primary reasons that we win there is because our solution is very flexible. It integrates well with their workflow. And it enables them to essentially pick and choose what they would like to do themselves and what they would like us to do on their behalf. So again, the revenue model is a licensing fee similar to other platform as a service models plus a per transaction fee.

Alexander Yearley Draper
SunTrust Robinson Humphrey, Inc., Research Division

Okay. And then just a quick follow-up on that. I would assume, Mark, that revenue is essentially and is probably going fast but immaterial to sort of where current total numbers are, is that accurate?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

That's correct.

Alexander Yearley Draper
SunTrust Robinson Humphrey, Inc., Research Division

Okay, great. And then one last follow-up. And I don't know if there's a way that you guys can track this. I assume you could, but when you look at the growth in utilization, one of the things that I'm curious and always trying to understand is how much is the market -- how much is also -- either word of mouth or repeat users? For customers you've had on 2, 3, 4 years, do you track? And are you willing to give us some stats on how often it's repeat users that are building a baseline and how often they're there? And is that a good way to think about the stickiness is you got existing users that may be once a year, twice a year, maybe it's every other year, keep coming back to use the technology?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, sure. So the numbers that we talk about are about 1.3 to 1.4 visits per user per year. So if you do the math on that, the unique users is about 70% of the total visit volume. Certainly, that increases over time. Word of mouth is very powerful and that's why when we talk about utilization among cohorts of our clients, we sort of talk about them as vintages. We see the utilization increase from the first year to the second year and even more from the second to the third and fourth year. So certainly, there's a benefit that we get from the maturing of our book of business over time, but still, the majority of our business has been -- of our clients had been with us less than 3 years. So we continue to get the benefit of that over time and when you combine that with our improvement and our ability to target communications to people, I think that's -- those 2 work together to help drive the improvement that we're seeing in our utilization rates.

Operator

Your next question comes from the line of Matthew Gillmor with Robert Baird.

Matthew Dale Gillmor
Robert W. Baird & Co. Incorporated, Research Division

I wanted to ask a couple of follow-ups on the utilization front. So Sean asked about some of the key drivers on the digital side and you also mentioned the flu season having an impact in the prepared remarks. Is there a way to tease out how much was driven by the flu season versus maybe the secular growth components from broader awareness?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, I would say this about the flu season. Although it was severe, it was short lived. So when we look at the flu season, usually, we get significant December effect and it lasts well into March. This year, we saw it pretty intensively in January and February but really not in December and March. So while it was more intense while it hits, it probably didn't have a significant of an overall impact because it was shorter and we didn't really see any impact of it, and in fact it dropped off in the very beginning of March. So I would say a small portion of that came from the cold and flu season, but the majority of it was a result of the communications. It's difficult for me to tease out the exact numbers on that, but I would say, directionally, that should give you the insight you need.

Matthew Dale Gillmor
Robert W. Baird & Co. Incorporated, Research Division

Got it, that's helpful. And Jason, you mentioned some of the employers shift away from the free model and maybe more towards the PEPM to drive utilization. Can you give us a flavor for what they're saying and why they're shifting back? And are you seeing any change in some of the competitor pricing behavior towards the PEPM model?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, absolutely. We're pleased to see that the market is becoming more rational, that our customers are understanding the value that we provide and the importance of driving utilization. And I would say from small accounts all the way to the largest accounts, we're seeing them realize that you get what you pay for. And if you're not paying anything, you're probably not getting anything. So we have seen the recognition and, in fact, we've seen clients come to us proactively. We've also seen some operational challenges amongst some of our other competitors in the market, which again is causing clients to -- who maybe made a different decision a couple of years ago to come to us. With respect to pricing, we're seeing, I would say, a more rational behavior. There's -- I think as companies have to go out and raise capital, they probably realize that they have to show more rational economic model, and certainly we've been the beneficiary of that. You can see our mix has been good, our PEPM pricing continues to be strong and I think everything from the clients to the consultants have really understood that all of this hinges on whether you can drive utilization.

Operator

Your next question comes of the line of Ryan Daniels of William Blair.

Ryan Scott Daniels
William Blair & Company L.L.C., Research Division

Jason, one for you. You mentioned at your client summit that your clients have more desire for you to help them work with more costly and complex medical conditions. I'm curious if you can talk a little bit more about what that might include? And then perhaps what operating model changes you might need to impart in order to manage more medically complex patients than what you're doing today?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, thanks, Ryan. Good catch on that. That was a strong theme that came through. We have historically played in the high-frequency low-severity end of the cost continuum. And I think our clients recognize that it's hard to reach people who are at the other end of that spectrum where it's lower frequency, higher severity and therefore, higher cost. And with the model like ours that has such high member satisfaction, they're looking to us to see if we can help them to address that other end of the continuum. When you ask about capabilities, I would say, we have been on the path to building those capabilities. And if you look at our progression, it's a very methodical one. So we started with acute episodic care with our -- what you would probably call virtual urgent care or our general medical product. When we added behavioral health, that took us into longitudinal care where we were managing a patient over a longer period of time frequently, somebody with multiple comorbidities. Our tobacco cessation program gave us the ability to bring in a nurse coach in addition to the treating physician. And then our dermatology program brings in a specialty network in addition to our behavioral health network. Finally, the addition of our labs enables us to send the patient for additional lab work and really creates more of an interaction with the member around their biometrics. So you put all of those together and it provides a lot of the building blocks for being able to help care for patients, whether in a primary or a secondary capacity over time and with much more complex cases. So while I will refrain from giving you specific conditions and/or products that we'll have in the market, I can tell you that we're actively looking at that moving up the continuum of care.

Ryan Scott Daniels
William Blair & Company L.L.C., Research Division

Okay, that's really helpful. And is that also a big impact on your utilization rates, meaning that while it's not just the short-term illnesses, the cold, the flu, the sinusitis, you're broadening, so therefore, the utilization rate is also going to naturally see upticks as more consumers access different types of solutions from Teladoc?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, so certainly, increasing utilization by offering a broader array of services is where in the middle of a strategy. And I think that manifests itself too is: One is the more you offer to a consumer, the more part of their overall health care you can take care of, but also, with our behavioral health, for example, people don't just have one visit, right? It's a series of visits with the provider. And so rather than 1.3 visits per person, you see significantly more in our behavioral health product.

Ryan Scott Daniels
William Blair & Company L.L.C., Research Division

Okay. And then maybe just a couple more. The Texas legislation written today, if that bill becomes law, would it require any material changes in the way you operate or deliver services for members in that state?

Jason Gorevic
Chief Executive Officer, President and Director

No. No changes at all would be required. The one change would be that we would be able to offer video in Texas where we don't today.

Ryan Scott Daniels
William Blair & Company L.L.C., Research Division

Okay. And then last one, not to leave Mark out, but just for guidance. If I look at the implied visits and membership kind of at the midpoints in revenue, it looks maybe a little bit larger jump in PMPM fees than normal. And I'm curious if that's just the impact of some of the SMB customers coming on or more of the visit included coming on that's going to push that up a little bit sequentially?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

Yes. Ryan, you hit on 1 of the 2. So it's the visits included, small-, medium-sized businesses are again attracted to that product. And then also the increase from those high subscription rates from our direct-to-consumer behavioral product, which, I think I've told you in the past, will exceed 15% of our 2017 revenue.

Operator

Your next question comes from the line of Mohan Naidu of Oppenheimer.

Mohan A. Naidu
Oppenheimer & Co. Inc., Research Division

Jason, going back to the earlier question about the selling season. Is there an improvement in clients' understanding of telehealth offering when you're going to the market right now? or -- and I guess, you don't need to stop from the beginning and convince them that you may need to get telehealth versus just going in and competing with other vendors?

Jason Gorevic
Chief Executive Officer, President and Director

Yes. Mo, thanks. I would say that's true in the large employer market. It's increasingly true in the health plan market. The small and midsized employer market, still a lot of education and, of course, we sell through a broker distribution channel there. So frequently, we're orienting the brokers and they're orienting their clients. And then in the provider space, there's -- that's still a lot of greenfield. That's a lot of new customers who are -- they may have a chief strategy officer who's leading the charge or, in many cases, now they're starting to have a telehealth officer at the hospital system who's starting to create a strategy around it.

Mohan A. Naidu
Oppenheimer & Co. Inc., Research Division

Got it, got it. One question around the specialty. So you stressed a lot on specialty on this call today. Is there something interesting going on with a lot of clients pulling ahead. You talked about a lot of interest from health plan clients? Why are they suddenly looking at specialty now? Are they seeing more data come out of your employer clients that convinces them to look at it?

Jason Gorevic
Chief Executive Officer, President and Director

I would say it's a combination of things. One is it's just the sort of the cycle of we've now been in market for a little while, we've been talking to our clients health plans and employers about it. And so, there's just sort of a natural maturation in progress that we're making there. I would say there is quite a bit of recognition of the challenge of mental health and, especially, untreated mental health and its impact on the cost of medical care as well as -- especially when they're co-morbid conditions. And then lastly, certainly, we have now proven ourselves and we have referenced clients that we can talk to and bring to bear for our prospects and so that certainly helps our ability to bring a prospect along to comfort and then ultimately going forward with implementation.

Operator
Your next question comes from the line of Richard Close of Canaccord Genuity.

Richard Collamer Close
Canaccord Genuity Limited, Research Division

Just wanted to dive in a little bit deeper on Ryan's question on the client summit and broadening the clinical service offering. Mark, I was wondering if you could just touch base and whether you move into those high cost areas, low frequency. Does that change the margin profile of the business at all? How are you thinking of that as you ramp up some of those new offerings in future years?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

Great question. We'd spent a lot of time looking at the relative margin variance and offering those services and we've modeled them out to the extent that we've guided people into that high 60s gross margin level. That's consistent with where we feel the business is going to go over the next couple of years. We continue to generate 70%, 72% upwards to 75% margins on the core business, but we see the contribution of those additional services likely contributing to us getting into that high-60%s range over the next couple of years.

Richard Collamer Close
Canaccord Genuity Limited, Research Division

Okay. Jason, you threw out TD Ameritrade there, I think you said 20% utilization, if I'm not mistaken. And can you just -- if that's the case, that's what they're utilization rate is. Can you just walk us through what they did or what you guys did with them to get 20%? And is that something we should think about long term for a majority of customers?

Jason Gorevic
Chief Executive Officer, President and Director

So TD Ameritrade has been a client for quite some time. They are enthusiastic supporters, we work closely with them, design and communications, to their employee base. They have strong internal champions. And I would say they're a good example of a model client. Having said that, at roughly 20% utilization, slightly above that, they're not unique. We have many clients in the 20% to even 50% utilization range. In fact, I had a client at our client summit that is at 81% utilization. So unfortunately, we can't get approval from every client to talk about them by name on a call like this, but when a client engages with us and really partners with us to drive awareness, drive utilization, it is very, very effective. And we're fortunate we had about 40 clients -- almost 40 clients at the summit and we get a lot of best practice sharing among them, which, quite frankly, is one of the most valuable parts of the summit. We learn from it and they learn from each other. We're starting to work on how we create better community among our clients so that they can do that on an ongoing basis, not just once a year at our client summit, and do it much more broadly by using technology and some of our capabilities to create more of a peer-to-peer best practice sharing because we think the network effect of our 7,500 plus clients can be very powerful.

Richard Collamer Close
Canaccord Genuity Limited, Research Division

Okay. And my final question, again, I missed utilization. As you think about the different segments, employer, payers, now you've got providers although, that is pretty new, can you just give us sort of a ballpark in terms of what average utilization rate is maybe for employer versus a payer? How we should think about that?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

Richard, without giving a range, you should expect the employers to continue to -- we characterize them as having both of the best opportunity to increase utilization but also experiencing the highest utilization among our members. And next is obviously, as a result of their tenure with them, the payers and clearly, those newer clients that are coming on, the providers, we'd expect to see them ramp up, clearly easy to see them double and triple over where they are today. But with regard to where they would rank, it's clearly the employers that will see the highest utilization coming from them.

Operator

Your next question comes from the line of Steven Wardell with Chardan Capital Markets.

Steven William Wardell
Chardan Capital Markets, LLC, Research Division

My first question is, do you expect provide visits that you get to provider customers to differ from visits that you get from employer customers? So you describe employer customers as high frequency, low acuity. What about the visit traffic that comes to you from providers? Do you think that will be substantially different?

Jason Gorevic
Chief Executive Officer, President and Director

I would say, in some cases, yes, and in some cases, no. And it very much is aligned with the strategy and the use cases that the providers are oriented to work. And let me give you the 2 ends of the spectrum. On one end of the spectrum, those that will be very similar to our existing or through more traditional book of business are those providers who are looking to use Teladoc as a way to improve their branding, improve their presence in the local market and create a funnel for members into their system and therefore, they put a cobranded product into the local market on more of a direct-to-consumer basis. So think about that as very similar to our general or medical product. On the other end of the spectrum, we're working with providers who see the Teladoc platform as a phenomenal opportunity, to better engage with patients post-acute, postsurgical, due post-discharge, plan adherence and follow-up and of course, those are very different. You have postsurgical patients and the follow-up is based on -- is more oriented towards how their recovery is going, checking their wounds, are they out on their meds? Is their weight stable? Things like that. So it really ranges depending on the use case and the priorities of the hospital system. But the nice thing about our platform, one of the reasons that we're having such success is that it really spans that -- it's flexible enough that it spans all of those use cases seamlessly.

Steven William Wardell
Chardan Capital Markets, LLC, Research Division

Great. And will you say you have customers who are fee for service and others that are fee for value in the provider world? And do they behave differently? Which you expect more business from the fee-for-value customers, for example?

Jason Gorevic
Chief Executive Officer, President and Director

I think it really dictates what their primary strategy is. So if someone -- if a provider is more fee-for-value oriented, if they're taking risk in an ACO type of relationship, then they're much more likely to focus on eliminating leakage outside of their system, managing their resource consumption and things like the discharge planning that I just described. If they're fee for service, they're probably more oriented toward increasing their volume and using Teladoc as a way to increase their patient flow.

Steven William Wardell
Chardan Capital Markets, LLC, Research Division

Great. And you mentioned the way that you engage with providers is through a software license with them. Does that mean that they stand up your software on their premises? Or are they simply sort of partaken in your hosted instance of the software?

Jason Gorevic
Chief Executive Officer, President and Director

It's the latter. We're not installing any software on their premises. It is entirely a cloud-based solution that we provide for them.

Operator

Your last question is from Matt Hewitt of Craig-Hallum Capital Group.

Matthew Gregory Hewitt
Craig-Hallum Capital Group LLC, Research Division

Two for me, actually. One, how does the cost for these varied targeted digital marketing campaigns differ from the more traditional approach that you've employed last couple of years?

Jason Gorevic
Chief Executive Officer, President and Director

It's really much more cost-effective because we can take up more of a rifle-shot approach rather than a shotgun approach. And so being able to target those who are most likely to respond in a digital fashion is -- obviously digital communication is a lot less expensive than direct mail, for example. And it would not be cost-effective if you couldn't do it in a targeted manner. But we have very sophisticated mechanisms to be able to do that and over the course of the last, I would say, 18 months, we've really significantly improved our ability to do it, to take advantage of the technology that is out there in the market and really become a state-of-the-art targeted marketer.

Matthew Gregory Hewitt
Craig-Hallum Capital Group LLC, Research Division

Okay. And then, one last one for me. Obviously, it could be a while before we have the final version, but the house passes the new health care bill. What, if any, impact could that version that I realized that there could be changes in the Senate, but is there anything that we should be focused on or paying attention to that could impact your business positively or negatively?

Jason Gorevic
Chief Executive Officer, President and Director

Yes, I would say -- I would echo what you said about the fact that there could be changes and we are unlikely to know what the final bill looks like. Having said that, I would say, generally, it's fairly natural for us. There are a couple of puts and takes, but I think eliminating the minimum benefit plan probably opens up opportunity for other kinds of products in the market into which Teladoc fits very nicely. At the same time, pulling back on some of the Medicaid membership. We don't have -- not much of our business now is Medicaid. And so I don't think you would see anything that looks like a contraction in our existing customer base. So I don't think that would have a significant impact on us as I look at our book of business today. Again, I think the bigger thing I would look at is there's generally positive regulatory momentum relative to telehealth, both in Washington and in the States. And we're much more likely to see benefit from that than we are to see any substantial impacts from the new health care bill or whatever that ends up looking like.

Operator

Your last question is from Richard Close of Canaccord Genuity.

Richard Collamer Close
Canaccord Genuity Limited, Research Division

On utilization, have you guys ever given any type of guidance in terms of the basis-point improvement you expect on an annual basis or any longer-term targets?

Mark J. Hirschhorn
Chief Financial Officer, Chief Operating Officer and Executive Vice President

We haven't guided towards any longer-term targets, however, we have suggested that as in the past, where we have seen the highest utilization come in over the last 3 years, coming in on Q4, we'd expect that ramp from Q1 to Q4 to be an increase of anywhere from 15% to 25%. As you can imagine, because of the seasonality, and as you can read into the numbers, we expect slightly lower visits completed in Q2 and Q3, and really the bulk of our visits coming in close to the 400,000 number in Q4 of this year.

Jason Gorevic
Chief Executive Officer, President and Director

So I think that concludes all the questions we have. I want to thank everybody for participating in today's call. As a final note, we also wanted to remind our shareholders that we filed our definitive proxy form as well as additional soliciting materials with the SEC, summarizing the Board of Directors' rationale for our 2017 shareholder proposals. We look forward to having you join our virtual Annual General Meeting on May 25, and I'd encourage you to reach out to Jisoo Suh with any follow-up questions.

And so with that, I think we'll close the call and, again, thanks, everybody, for joining today.

OperatorThis concludes today's conference call. You may now disconnect.