ALLIANCE IMAGING INC /DE/
Form 10-Q
May 09, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For Quarter Ended: March 31, 2008

Commission File Number: 1-16609

ALLIANCE IMAGING, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**33-0239910**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

1900 South State College Boulevard
Suite 600
Anaheim, California 92806
(Address of principal executive office)

(714) 688-7100
(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 ý No o

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

Large accelerated filer o	Accelerated filer ý	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller 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 ý

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of April 30, 2008:

Common Stock, $.01 par value, 51,032,021 shares

ALLIANCE IMAGING, INC.

FORM 10-Q

March 31, 2008

Index

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALLIANCE IMAGING, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(in thousands)

	December 31, 2007	March 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 120,892	$ 107,199
Accounts receivable, net of allowance for doubtful accounts	58,439	61,231
Deferred income taxes	16,091	16,091
Prepaid expenses and other current assets	5,637	3,732
Other receivables	7,304	6,069
Total current assets	208,363	194,322
Equipment, at cost	777,212	801,290
Less accumulated depreciation	(434,364)	(448,579)
Equipment, net	342,848	352,711
Goodwill	175,804	175,620
Other intangible assets, net	93,221	93,049
Deferred financing costs, net	8,460	8,538
Other assets	21,111	19,384
Total assets	$ 849,807	$ 843,624
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable	$ 20,622	$ 12,506
Accrued compensation and related expenses	17,976	18,697
Accrued interest payable	4,912	9,540
Other accrued liabilities	33,512	37,644
Current portion of long-term debt	3,627	3,599
Total current liabilities	80,649	81,986
Long-term debt, net of current portion	376,184	361,916
Senior subordinated notes	290,985	291,446
Minority interests and other liabilities	6,271	9,207
Deferred income taxes	92,062	92,120
Total liabilities	846,151	836,675
Commitments and contingencies (Note 12)		
Stockholders' equity:		

	December 31, 2007	March 31, 2008
Common stock	509	509
Treasury stock	(61)	(61)
Additional paid-in (deficit) capital	(1,470)	149
Accumulated comprehensive income (loss)	205	(1,533)
Retained earnings	4,473	7,885
Total stockholders' equity	3,656	6,949
Total liabilities and stockholders' equity	$ 849,807	$ 843,624

See accompanying notes.

3

ALLIANCE IMAGING, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

AND COMPREHENSIVE INCOME

(Unaudited)

(in thousands, except per share amounts)

	Quarter Ended March 31, 2007	Quarter Ended March 31, 2008
Revenues	$ 109,406	$ 119,121
Costs and expenses:		
Cost of revenues, excluding depreciation and amortization	56,177	62,782
Selling, general and administrative expenses	14,728	15,709
Severance and related costs	76	147
Depreciation expense	20,801	21,413
Amortization expense	1,210	1,857
Interest expense, net of interest income	10,074	11,816
Other (income) and expense, net	(320)	(62)
Total costs and expenses	102,746	113,662
Income before income taxes, minority interest expense and earnings from unconsolidated investees	6,660	5,459
Income tax expense	3,952	2,677
Minority interest expense	521	594
Earnings from unconsolidated investees	(3,484)	(1,224)
Net income	$ 5,671	$ 3,412
Comprehensive income, net of taxes:		
Net income	$ 5,671	$ 3,412
Unrealized loss on hedging transactions, net of taxes	(269)	(1,738)
Comprehensive income	$ 5,402	$ 1,674
Earnings per common share:		
Basic	$ 0.11	$ 0.07
Diluted	$ 0.11	$ 0.07
Weighted average number of shares of common stock and common stock equivalents:		
Basic	49,955	50,312
Diluted	51,088	51,986

See accompanying notes.

ALLIANCE IMAGING, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)

	Quarter Ended March 31,	
	2007	**2008**
Operating activities:		
Net income	$ 5,671	$ 3,412
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for doubtful accounts	832	1,509
Share-based payment	898	1,526
Depreciation and amortization	22,011	23,270
Amortization of deferred financing costs	397	569
Accretion of discount on senior subordinated notes		461
Adjustment of derivatives to fair value	672	
Distributions (less than) greater than equity in undistributed income of investees	(421)	76
Deferred income taxes	2,844	1,235
Excess tax benefit from share-based payment arrangements	(254)	(20)
Gain on sale of assets	(320)	(62)
Changes in operating assets and liabilities:		
Accounts receivable	(3,307)	(4,301)
Prepaid expenses and other current assets	464	1,905
Other receivables	(1,831)	1,235
Other assets	(1,128)	380
Accounts payable	(4,228)	(8,394)
Accrued compensation and related expenses	(1,260)	721
Accrued interest payable	2,657	4,628
Income taxes payable	(637)	
Other accrued liabilities	333	(209)
Minority interests and other liabilities	1,299	381
Net cash provided by operating activities	24,692	28,322
Investing activities:		
Equipment purchases	(24,764)	(16,975)
Decrease in deposits on equipment	13,455	1,209
Acquisitions, net of cash received		(10,799)
Proceeds from sale of assets	1,392	1,045
Net cash used in investing activities	(9,917)	(25,520)
Financing activities:		
Principal payments on equipment debt	(855)	(941)
Proceeds from equipment debt	138	
Principal payments on term loan facility	(600)	(15,000)
Principal payments on revolving loan facility	(7,000)	
Proceeds from revolving loan facility	7,000	
Payments of debt issuance costs	(127)	(647)
Proceeds from exercise of employee stock options	556	73
Excess tax benefit from share-based payment arrangements	254	20
Net cash used in financing activities	(634)	(16,495)

	Quarter Ended March 31,	
Net increase (decrease) in cash and cash equivalents	14,141	(13,693)
Cash and cash equivalents, beginning of period	16,440	120,892
Cash and cash equivalents, end of period	$ 30,581	$ 107,199
Supplemental disclosure of cash flow information:		
Interest paid	$ 6,587	$ 7,157
Income taxes paid, net of refunds	937	1,075
Supplemental disclosure of non-cash investing and financing activities:		
Net book value of assets exchanged	$ 938	$ 27
Capital lease obligations assumed for the purchase of equipment debt		1,645
Comprehensive loss from hedging transactions, net of taxes	(269)	(1,738)
Deposits on equipment in accounts payable	3,877	278

See accompanying notes.

ALLIANCE IMAGING, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2008
(Unaudited)
(Dollars in thousands, except per share amounts)

1. Basis of Presentation, Principles of Consolidation, and Use of Estimates

Basis of Presentation The accompanying unaudited condensed consolidated financial statements have been prepared by Alliance Imaging, Inc. (the "Company") in accordance with accounting principles generally accepted in the United States of America and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (including normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the quarter ended March 31, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes to the consolidated financial statements for the year ended December 31, 2007.

Principles of Consolidation The accompanying unaudited condensed consolidated financial statements of the Company include the assets, liabilities, revenues and expenses of all majority owned subsidiaries over which the Company exercises control. Intercompany transactions have been eliminated. We record minority interest expense related to our consolidated subsidiaries which are not wholly owned. Investments in non-consolidated investees are accounted for under the equity method.

Use of Estimates The preparation of condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

2. Transactions

Effective October 1, 2007, the Company purchased the assets of Diagnostic Radiology Systems, Inc., a mobile provider of MRI and PET/CT, with operations in a certificate of need state. The purchase price consisted of $8,620 in cash and transaction costs. The acquisition was financed using internally generated funds. As a result of this acquisition, the Company recorded goodwill of $2,148 and acquired intangible assets of $2,240, of which $1,520 was assigned to customer contracts, which is amortized over eight years, $510 was assigned to the non-compete agreement, which is amortized over one year, and $210 was assigned to certificates of needs, which have indefinite useful lives and are not subject to amortization. The intangible assets were recorded at fair value at the acquisition date. All recorded goodwill and intangible assets are capitalized for tax purposes and amortized over 15 years. The preliminary values above are subject to adjustment for up to one year after the close of the transaction as additional information is obtained, and those adjustments could be significant. The year ended December 31, 2007 included three months of operations from this acquisition. During the quarter ended March 31, 2008, the Company increased goodwill by $7 as a result of changes in the original valuation of assets and liabilities acquired. The Company has not included pro forma information as this acquisition did not have a material impact on its consolidated financial position or results of operations.

Effective November 2, 2007, Alliance Oncology ("AO") purchased the assets of eight radiation therapy centers in Alabama, Arkansas, Mississippi, and Missouri from Bethesda Resources, Inc., a wholly-owned subsidiary of Sonix, Inc. Many of these centers are sole community providers and are located on or near hospital campuses. Several of these radiation therapy centers operate under certificates of need. The purchase price consisted of $36,500 in cash and $800 in assumed liabilities and transaction costs. The acquisition was financed using internally generated funds and capital leases. As a result of this acquisition, the Company recorded goodwill of $4,246 and acquired intangible assets of $31,230, of which $2,230 was assigned to the physician network, which is amortized over seven years and $29,000 was assigned to certificates of needs, which have indefinite useful lives and are not subject to amortization. The intangible assets were recorded at fair value at the acquisition date. All recorded goodwill and intangible assets are capitalized for tax purposes and amortized over 15 years. The preliminary values above are subject to adjustment for up to one year after the close of the transaction as additional information is obtained, and those adjustments could be significant. During the quarter ended March 31, 2008, the company decreased goodwill by $81 as a result of changes in the original valuation of assets and liabilities acquired. The year ended December 31, 2007 included approximately two months of operations from this acquisition. The Company has not included pro forma information as this acquisition did not have a material impact on its consolidated financial position or results of operations.

Effective November 5, 2007, the Company purchased all of the outstanding shares of the New England Health Enterprises Business Trust and all of the outstanding membership interests of New England Imaging Management, LLC, a fixed-site provider of MRI and CT, collectively referred to as New England Health Enterprises, or NEHE. NEHE operates seven fixed-site imaging centers and one mobile MRI system in Maine and Massachusetts. The total purchase price was $46,905, which consisted of $44,635 in cash, $2,270 in cash which is being held in an escrow account, and $4,592 in assumed liabilities and transaction costs. The acquisition was financed using internally generated funds, borrowings under an Acquisition Credit Facility and capital leases. The Company recorded total goodwill of $19,341, which includes $10,947 of goodwill related to deferred tax liabilities recorded for basis differences in intangible assets as a result of the acquisition. None of the goodwill recorded is deductible for tax purposes. The Company acquired intangible assets of $29,000, of which $15,700 was assigned to the physician network, which is amortized over 15 years, $3,800 was assigned to the non-compete agreement, which is amortized over five years, and $9,500 was assigned to certificates of need held by NEHE, which have indefinite useful lives and are not subject to amortization. These assets were recorded at fair value at the acquisition date. The acquisition also included $2,270 for a contingent payment which is being held in an escrow account, pending the resolution of claims for indemnification and contingent consideration based on certain performance target requirements, which will be resolved over the next one to three years. When the contingencies are resolved and consideration is distributable from the escrow account, the Company will record the fair value of the consideration as additional purchase price to goodwill. The preliminary values above are subject to adjustment for up to one year after the close of the transaction as additional information is obtained, and those adjustments could be significant. During the quarter ended March 31, 2008, the Company decreased goodwill by $110 as a result of changes in the original valuation of assets and liabilities acquired. The year ended December 31, 2007 included approximately two months of operations from this acquisition. The Company has not included pro forma information as this acquisition did not have a material impact on its consolidated financial position or results of operations.

In the first quarter of 2008, the Company purchased six CyberKnife® robotic radiosurgery systems from Accuray, Inc. The radiosurgery systems are currently providing radiosurgery services at hospitals located in California, Maryland, New Jersey and Tennessee. The total purchase price was $11,937 in cash, of which $1,098 will be paid during the second quarter of 2008 and $672 in transaction costs. The acquisition was financed using proceeds from the Company's issuance of additional 7.25% senior subordinated notes in December 2007. As a result of this acquisition, the Company recorded acquired intangible assets of $1,675, which was assigned to customer contracts and will be amortized over seven years. The intangible assets were recorded at fair value at the acquisition date. All recorded intangible assets are capitalized for tax purposes and amortized over 15 years. The preliminary values above are subject to adjustment for up to one year after the close of the transaction as additional information is obtained, and those adjustments could be significant. The quarter ended March 31, 2008 included an immaterial amount from operations from this acquisition. The Company has not included pro forma information as this acquisition did not have a material impact on its consolidated financial position or results of operations.

3. Share-Based Compensation

The Company adopted Statement of Financial Accounting Standards No. 123(R) (Revised December 2004), "Share-Based Payment" ("SFAS 123(R)"), in the fiscal year beginning January 1, 2006, using the modified prospective application transition method. Under SFAS 123(R), the Company records in its consolidated statements of operations (i) compensation costs for options granted, modified, repurchased or cancelled on or after January 1, 2006 under the provisions of SFAS 123(R) and (ii) compensation costs for the unvested portion of options granted prior to January 1, 2006 over their remaining vesting periods using the amounts previously measured under SFAS 123 for pro forma disclosure purposes.

In November 2005, the Financial Accounting Standards Board ("FASB") issued FASB Staff Position ("FSP") FAS 123R-3, "Transition Election to Accounting for the Tax Effects of Share-Based Payment Awards" ("FSP FAS 123R-3"). The Company has elected to follow the alternative transition method as described in FSP FAS 123R-3 for computing its additional paid-in capital pool. In addition, the Company treats the tax deductions from stock options as being realized when they reduce taxes payable in accordance with the principles and timing under the relevant tax law.

Stock Option Plans and Awards

In November 1999, the Company adopted an employee stock option plan (the "1999 Equity Plan") pursuant to which options and awards with respect to a total of 6,325,000 shares of the Company's common stock became available for grant. On May 30, 2007, the Company adopted an amendment to the 1999 Equity Plan which increased the number of shares available to be awarded to 8,025,000 shares. As of March 31, 2008, a total of 1,249,748 shares are available for grant under the 1999 Equity Plan. Options are granted with exercise prices equal to fair value of the Company's common stock at the date of grant, except as noted below. All options have 10-year terms. Options granted after January 1, 2008 are time options which vest 25% each year, over four years. For options granted prior to January 1, 2008, initial stock option grants were comprised 50% of "time options" and 50% of "performance options." The time options have a five-year vesting schedule, vesting 20% per year. The performance options cliff vest after eight years, however, in the event certain operating performance targets are met, up to 20% of the performance options may vest each year, accelerating the vesting period up to five years. Subsequent stock options granted under the 1999 Equity Plan to employees are always time options which vest 5% in the first year, 20% in the second year and 25% in years three through five.

In November 2000, the Company granted stock options to certain employees at exercise prices below the fair value of the Company's common stock, of which 35,000 options were outstanding at March 31, 2008. The exercise prices of these options and the fair value of the Company's common stock on the grant date were $5.60 and $9.52 per share, respectively.

The Company is using the Black-Scholes option pricing model to value the compensation expense associated with stock-based awards. The fair value of each option award is estimated on the date of grant using the Black-Scholes option pricing model that uses the assumptions noted in the table below. In addition, forfeitures are estimated when recognizing compensation expense, and the estimate of forfe