RadNet, Inc.
Form 10-Q
August 09, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2012

OR

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

For the transition period from __________ to __________

Commission File Number 0-19019

RadNet, Inc.

(Exact name of registrant as specified in charter)

Delaware	**13-3326724**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
1510 Cotner Avenue	
Los Angeles, California	**90025**
(Address of principal executive offices)	**(Zip Code)**

(310) 478-7808

(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 and 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 x No ¨

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

Large accelerated filer ¨	Accelerated filer x	Non-accelerated filer ¨ (do not check if a smaller reporting company)	Smaller reporting company ¨

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

The number of shares of the registrant's common stock outstanding on August 3, 2012, was 38,340,482 shares.

RADNET, INC.

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PART I - FINANCIAL INFORMATION

RADNET, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS EXCEPT SHARE DATA)

	June 30, 2012 (unaudited)	December 31, 2011
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 234	$ 2,455
Accounts receivable, net	131,443	128,432
Asset held for sale	–	2,300
Prepaid expenses and other current assets	21,171	19,140
Total current assets	152,848	152,327
PROPERTY AND EQUIPMENT, NET	219,044	215,527
OTHER ASSETS		
Goodwill	166,160	159,507
Other intangible assets	51,483	53,105
Deferred financing costs, net	11,948	13,490
Investment in joint ventures	23,119	22,326
Deposits and other	3,007	2,906
Total assets	$ 627,609	$ 619,188
LIABILITIES AND EQUITY DEFICIT		
CURRENT LIABILITIES		
Accounts payable, accrued expenses and other	$ 109,039	$ 103,101
Due to affiliates	4,490	3,762
Deferred revenue	1,008	1,076
Current portion of notes payable	6,275	6,608
Current portion of deferred rent	1,023	999
Current portion of obligations under capital leases	4,607	6,834
Total current liabilities	126,442	122,380
LONG-TERM LIABILITIES		
Deferred rent, net of current portion	14,965	12,407
Deferred taxes	277	277
Line of credit	59,500	58,000
Notes payable, net of current portion	481,267	484,046
Obligations under capital lease, net of current portion	2,282	3,338

Other non-current liabilities	7,834	8,547
Total liabilities	692,567	688,995
COMMITMENTS AND CONTINGENCIES		
EQUITY DEFICIT		
Common stock - $.0001 par value, 200,000,000 shares authorized; 38,340,482, and 37,426,460 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively	4	4
Paid-in-capital	167,385	165,796
Accumulated other comprehensive loss	(369)	(946)
Accumulated deficit	(232,775)	(235,610)
Total RadNet, Inc.'s equity deficit	(65,755)	(70,756)
Noncontrolling interests	797	949
Total equity deficit	(64,958)	(69,807)
Total liabilities and equity deficit	$ 627,609	$ 619,188

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

RADNET, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(IN THOUSANDS EXCEPT SHARE DATA)

(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
NET SERVICE FEE REVENUE				
Service fee revenue, net of contractual allowances and discounts	$171,746	$153,370	$340,246	$297,453
Provision for bad debts	$(6,395)	(5,671)	(12,879)	(10,702)
Net service fee revenue	165,351	147,699	327,367	286,751
OPERATING EXPENSES				
Cost of operations	136,554	119,113	271,954	234,941
Depreciation and amortization	14,893	14,296	29,785	28,217
Loss (gain) on sale and disposal of equipment	276	(1,356)	300	(1,597)
Severance costs	163	509	612	654
Total operating expenses	151,886	132,562	302,651	262,215
INCOME FROM OPERATIONS	13,465	15,137	24,716	24,536
OTHER EXPENSES				
Interest expense	13,475	13,150	27,042	26,065
Other income	(1,344)	(689)	(2,491)	(2,060)
Total other expenses	12,131	12,461	24,551	24,005
INCOME BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF JOINT VENTURES	1,334	2,676	165	531
Provision for income taxes	(421)	(337)	(666)	(484)
Equity in earnings of joint ventures	1,986	1,267	3,248	2,751
NET INCOME	2,899	3,606	2,747	2,798
Net (loss) income attributable to noncontrolling interests	(47)	85	(88)	153
NET INCOME ATTRIBUTABLE TO RADNET, INC. COMMON STOCKHOLDERS	$2,946	$3,521	$2,835	$2,645
BASIC NET INCOME PER SHARE ATTRIBUTABLE TO RADNET, INC. COMMON STOCKHOLDERS	$0.08	$0.09	$0.08	$0.07
DILUTED NET INCOME PER SHARE ATTRIBUTABLE TO RADNET, INC. COMMON	$0.07	$0.09	$0.07	$0.07

STOCKHOLDERS				
WEIGHTED AVERAGE SHARES OUTSTANDING				
Basic	37,761,316	37,357,840	37,715,723	37,308,038
Diluted	39,430,716	39,820,163	39,215,632	39,376,958

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

RADNET, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(IN THOUSANDS)

(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
NET INCOME	$2,946	$3,521	$2,835	$2,645
Foreign currency translation adjustments	20	30	26	35
Reclassification of net cash flow hedge losses included in net income during the period	275	306	551	612
COMPREHENSIVE INCOME	3,241	3,857	3,412	3,292
Less comprehensive (loss) income attributable to non-controlling interests	(47)	85	(88)	153
COMPREHENSIVE INCOME ATTRIBUTABLE TO RADNET, INC. COMMON STOCKHOLDERS	$3,194	$3,942	$3,324	$3,445

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

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RADNET, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF EQUITY DEFICIT

(IN THOUSANDS EXCEPT SHARE DATA)

(unaudited)

	Common Stock		Paid-in	Accumulated	Accumulated Other Comprehensive	Total RadNet, Inc's Equity	Noncontrolling	Total Equity
	Shares	Amount	Capital	Deficit	Loss	Deficit	Interests	Deficit
BALANCE - JANUARY 1, 2012	37,426,460	$ 4	$ 165,796	$ (235,610)	$ (946)	$ (70,756)	$ 949	$ (69,807)
Issuance of common stock upon exercise of options/warrants	74,022	–	–	–	–	–	–	–
Stock-based compensation	–	–	1,706	–	–	1,706	–	1,706
Purchase of non-controlling interests	–	–	(117)	–	–	(117)	–	(117)
Issuance of restricted stock	840,000	–	–	–	–	–	–	–
Dividends paid to noncontrolling interests	–	–	–	–	–	–	(64)	(64)
Change in cumulative foreign currency translation adjustment	–	–	–	–	26	26	–	26
Change in fair value of cash flow hedge from prior periods reclassified to earnings	–	–	–	–	551	551	–	551
Net income (loss)	–	–	–	2,835	–	2,835	(88)	2,747
BALANCE - JUNE 30, 2012	38,340,482	$ 4	$ 167,385	$ (232,775)	$ (369)	$ (65,755)	$ 797	$ (64,958)

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

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RADNET, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (IN THOUSANDS)

(unaudited)

	Six Months Ended June 30, 2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$2,747	$2,798
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	29,785	28,217
Provision for bad debt	12,879	10,702
Equity in earnings of joint ventures	(3,248)	(2,751)
Distributions from joint ventures	3,375	2,370
Deferred rent amortization	2,582	1,310
Amortization of deferred financing cost	1,542	1,467
Amortization of bond discount	132	119
Loss (gain) on sale and disposal of equipment	300	(1,597)
Amortization of cash flow hedge	551	612
Stock-based compensation	1,706	1,790
Changes in operating assets and liabilities, net of assets acquired and liabilities assumed in purchase transactions:		
Accounts receivable	(14,097)	(30,514)
Other current assets	(1,887)	(1,363)
Other assets	(29)	(227)
Deferred revenue	(68)	(230)
Accounts payable, accrued expenses and other	4,547	10,164
Net cash provided by operating activities	40,817	22,867
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of imaging facilities	(9,917)	(11,529)
Purchase of property and equipment	(25,347)	(24,915)
Proceeds from insurance claims on damaged equipment	—	2,469
Proceeds from sale of equipment	446	291
Proceeds from sale of imaging facilities	2,300	—
Purchase of equity interest in joint ventures	(920)	(1,500)
Net cash used in investing activities	(33,438)	(35,184)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on notes and leases payable	(8,016)	(10,602)
Deferred financing costs	—	(217)
Proceeds from, net of payments on, line of credit	1,500	25,700
Payments to counterparties of interest rate swaps, net of amounts received	(3,046)	(3,219)
Distributions to noncontrolling interests	(64)	(71)
Proceeds from issuance of common stock upon exercise of options/warrants	—	242
Net cash (used in) provided by financing activities	(9,626)	11,833

EFFECT OF EXCHANGE RATE CHANGES ON CASH	26	35
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,221)	(449)
CASH AND CASH EQUIVALENTS, beginning of period	2,455	627
CASH AND CASH EQUIVALENTS, end of period	$234	$178
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the period for interest	$24,451	$23,229

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

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RADNET, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

(unaudited)

Supplemental Schedule of Non-Cash Investing and Financing Activities

We acquired equipment and certain leasehold improvements for approximately $12.5 million and $10.0 million during the six months ended June 30, 2012 and 2011, respectively, that we had not paid for as of June 30, 2012 and 2011, respectively. The offsetting amount due was recorded in our condensed consolidated balance sheet under “accounts payable, accrued expenses and other.”

As discussed in Note 5, we entered into interest rate swap modifications in the first quarter of 2009. These modifications include a significant financing element and, as such, all cash inflows and outflows subsequent to the date of modification are presented as financing activities. Also, as a result of our debt refinancing completed on April 6, 2010, our interest rate swaps are no longer effective. Accordingly, all changes in their fair value after April 6, 2010 are, and will continue to be recognized in earnings as other expense.

Detail of investing activity related to acquisitions can be found in Note 2.

RADNET, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

NOTE 1 – NATURE OF BUSINESS AND BASIS OF PRESENTATION

At June 30, 2012, we operated a group of regional networks comprised of 237 centers, which we operate directly or indirectly through joint ventures located in seven states with operations primarily in California, Maryland, Florida, Delaware, New Jersey, Rhode Island and New York. We provide diagnostic imaging services including magnetic resonance imaging (MRI), computed tomography (CT), positron emission tomography (PET), nuclear medicine, mammography, ultrasound, diagnostic radiology, or X-ray, fluoroscopy and other related procedures. Our operations comprise a single segment for financial reporting purposes.

The consolidated financial statements include the accounts of Radnet Management, Inc. (or “Radnet Management”) and Beverly Radiology Medical Group III, a professional partnership (“BRMG”). The consolidated financial statements also include Radnet Management I, Inc., Radnet Management II, Inc., Radiologix, Inc., Radnet Managed Imaging Services, Inc., Delaware Imaging Partners, Inc., New Jersey Imaging Partners, Inc. and Diagnostic Imaging Services, Inc. (“DIS”), all wholly owned subsidiaries of Radnet Management. All of these affiliated entities are referred to collectively as “RadNet”, “we”, “us”, “our” or the “Company” in this report.

Accounting Standards Codification (“ASC”) Section 810-10-15-14 stipulates that generally any entity with a) insufficient equity to finance its activities without additional subordinated financial support provided by any parties, or b) equity holders that, as a group, lack the characteristics specified in the ASC which evidence a controlling financial interest, is considered a Variable Interest Entity (“VIE”). We consolidate all VIE’s in which we own a majority voting interest and all VIE’s for which we are the primary beneficiary. We determine whether we are the primary beneficiary of a VIE through a qualitative analysis that identifies which variable interest holder has the controlling financial interest in the VIE. The variable interest holder who has both of the following has the controlling financial interest and is the primary beneficiary: (1) the power to direct the activities of the VIE that most significantly impact the VIE’s economic performance and (2) the obligation to absorb losses of, or the right to receive benefits from, the VIE that could potentially be significant to the VIE. In performing our analysis, we consider all relevant facts and circumstances, including: the design and activities of the VIE, the terms of the contracts the VIE has entered into, the nature of the VIE’s variable interests issued and how they were negotiated with or marketed to potential investors, and which parties participated significantly in the design or redesign of the entity.

Howard G. Berger, M.D. is our President and Chief Executive Officer, a member of our Board of Directors and is deemed to be the beneficial owner, directly and indirectly, of approximately 14.1% of our outstanding common stock as of June 30, 2012. Dr. Berger also owns, indirectly, 99% of the equity interests in BRMG. BRMG provides all of the professional medical services at the majority of our facilities located in California under a management agreement with us, and employs physicians or contracts with various other independent physicians and physician groups to provide the professional medical services at most of our other California facilities. We generally obtain professional medical services from BRMG in California, rather than provide such services directly or through subsidiaries, in order to comply with California's prohibition against the corporate practice of medicine. However, as a result of our close relationship with Dr. Berger and BRMG, we believe that we are able to better ensure that medical service is provided at our California facilities in a manner consistent with our needs and expectations and those of our referring physicians, patients and payers than if we obtained these services from unaffiliated physician groups. BRMG is a partnership of ProNet Imaging Medical Group, Inc., Breastlink Medical Group, Inc. and Beverly Radiology Medical Group, Inc., each of which are 99% or 100% owned by Dr. Berger. RadNet provides non-medical, technical and administrative services to BRMG for which it receives a management fee, pursuant to the terms of the management agreement. Through the management agreement and our relationship with Dr. Berger, we have exclusive authority over all non-medical decision making related to the ongoing business operations of BRMG. Through our management agreement with BRMG we determine the annual budget of BRMG and make all physician employment decisions. BRMG has insignificant operating assets and liabilities, and de minimis equity. Through the management agreement with us, all of BRMG's cash flows are transferred to us. We have determined that BRMG is a VIE, and that we are the primary beneficiary, and consequently, we consolidate the revenue and expenses of BRMG. BRMG recognized $13.5 million and $15.1 million, and $26.2 million and $27.8 million of net revenues for the three and six months ended June 30, 2012 and 2011, respectively, and 13.5 million and 13.5 million, and $26.2 million and $26.6 million of operating expenses for the three and six months ended June 30, 2012 and 2011, respectively. RadNet recognized $53.6 million and $51.1 million, and $104.0 million and $98.9 million of net revenues for the three and six months ended June 30, 2012 and 2011, respectively, for management services provided to BRMG relating primarily to the technical portion of total billed revenue. The cash flows of BRMG are included in the accompanying condensed consolidated statements of cash flows. All intercompany balances and transactions have been eliminated in consolidation. The creditors of BRMG do not have recourse to our general credit and there are no other arrangements that could expose us to losses. However, BRMG is managed to recognize no net income or net loss and, therefore, RadNet may be required to provide financial support to cover any operating expenses in excess of operating revenues.

Aside from centers in California where we contract with BRMG for the provision of professional medical services and consolidate 100% of the patient service revenue, at the remaining centers in California and at all of the centers which are located outside of California, we have entered into long-term contracts with independent radiology groups in the area to provide physician services at those facilities. These third party radiology practices provide professional services, including supervision and interpretation of diagnostic imaging procedures, in our diagnostic imaging centers. The radiology practices maintain full control over the provision of professional services. The contracted radiology practices generally have outstanding physician and practice credentials and reputations; strong competitive market positions; a broad sub-specialty mix of physicians; a history of growth and potential for continued growth. In these facilities we enter into long-term agreements with radiology practice groups (typically 40 years). Under these arrangements, we provide management services and receive a fee which includes 100% of the technical reimbursements associated with imaging procedures for the use of our diagnostic imaging equipment and the provision of technical services. Our service fees also include a portion of the practice group's professional revenue, including revenue derived outside of our diagnostic imaging centers as well as fees for administrative services. The radiology practice groups retain the professional reimbursements associated with imaging procedures after deducting service fees paid to us. We have no financial controlling interest in the independent (non-BRMG) radiology practices; accordingly, we do not consolidate the financial statements of those practices in our consolidated financial statements and record only our service fee revenue.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and, therefore, do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with U.S. generally accepted accounting principles complete financial statements; however, in the opinion of our management, all adjustments consisting of normal recurring adjustments necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods ended June 30, 2012 and 2011 have been made. The results of operations for any interim period are not necessarily indicative of the results for a full year. These interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes thereto contained in our annual report on Form 10-K for the year ended December 31, 2011.

Significant accounting policies

For the period covered in this report, there have been no material changes to the significant accounting policies we use, and have explained, in our annual report on Form 10-K for the fiscal year ended December 31, 2011 with the exception of the following:

Revenues

Service fee revenue, net of contractual allowances and discounts, consists of net patient fees received from various payers and patients themselves based mainly upon established contractual billing rates, less allowances for contractual adjustments. As it relates to BRMG centers, this service fee revenue includes payments for both the professional medical interpretation revenue recognized by BRMG as well as the payment for all other aspects related to our providing the imaging services, for which we earn management fees from BRMG. As it relates to non-BRMG centers, this service fee revenue is earned through providing the use of our diagnostic imaging equipment and the provision of technical services as well as providing administration services such as clerical and administrative personnel, bookkeeping and accounting services, billing and collection, provision of medical and office supplies, secretarial, reception and transcription services, maintenance of medical records, and advertising, marketing and promotional activities.

Service fee revenues are recorded during the period the services are provided based upon the estimated amounts due from the patients and third-party payers. Third-party payers include federal and state agencies (under the Medicare and Medicaid programs), managed care health plans, commercial insurance companies and employers. Estimates of contractual allowances under managed care health plans are based upon the payment terms specified in the related contractual agreements. Contractual payment terms in managed care agreements are generally based upon predetermined rates per discounted fee-for-service rates. We also record a provision for doubtful accounts (based primarily on historical collection experience) related to patients and copayment and deductible amounts for patients who have health care coverage under one of our third-party payers.

Our service fee revenue, net of contractual allowances and discounts less the provision for bad debts for the three and six months ended June 30, are summarized in the following table (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Commercial Insurance/Managed Care Capitation	$115,332	$104,297	$228,788	$201,255
Medicare	34,500	29,842	68,107	58,410
Medicaid	5,833	4,924	11,572	9,831
Workers Compensation/Personal Injury	7,500	6,416	14,878	13,012
Other	8,581	7,891	16,901	14,945
Service fee revenue, net of contractual allowances and discounts	171,746	153,370	340,246	297,453
Provision for bad debts	(6,395)	(5,671)	(12,879)	(10,702)
Net service fee revenue	$165,351	$147,699	$327,367	$286,751

The break-out of our service fee revenue, net of contractual allowances and discounts, is calculated based upon global payments received from consolidated imaging centers from dates of service from each respective period illustrated.

Provision for Bad Debts

Although outcomes vary, our policy is to attempt to collect amounts due from patients, including co-payments and deductibles due from patients with insurance, at the time of service. We provide for an allowance against accounts receivable that could become uncollectible by establishing an allowance to reduce the carrying value of such receivables to their estimated net realizable value. We estimate this allowance based on the aging of our accounts receivable by each type of payer over an 18-month look-back period, and other relevant factors. A significant portion of our provision for bad debt relates to co-payments and deductibles owed to us by patients with insurance. There are various factors that can impact collection trends, such as changes in the economy, which in turn have an impact on the increased burden of co-payments and deductibles to be made by patients with insurance. These factors continuously change and can have an impact on collection trends and our estimation process.

Reclassifications

Certain reclassifications have been made to the three and six months ended June 30, 2011 consolidated financial statements and accompanying notes to conform with the three and six months ended June 30, 2012 presentation. Additionally, we have adjusted the prior year’s presentation as a result of the adoption of ASU 2011-07, Health Care

Entities (Topic 954). In connection with this adjustment, we identified certain mechanical errors in our historical calculation of the provision for bad debts, resulting in the gross up of the provision for bad debts and revenues by $3.1 million and $6.0 million for the three and six months ended June 30, 2011, respectively. The error has been corrected in these financial statements and upon adoption of the new guidance, resulted in no impact to net service fee revenue.

Liquidity and Capital Resources

We had a working capital balance of $26.4 million and $30.0 million at June 30, 2012 and December 31, 2011, respectively. We had net income attributable to RadNet, Inc.'s common stockholders of $2.8 million and $2.6 million for the six months ended June 30, 2012 and 2011, respectively. We also had an equity deficit of $65.0 million and $69.8 million at June 30, 2012 and December 31, 2011, respectively.

We operate in a capital intensive, high fixed-cost industry that requires significant amounts of capital to fund operations. In addition to operations, we require a significant amount of capital for the initial start-up and development expense of new diagnostic imaging facilities, the acquisition of additional facilities and new diagnostic imaging equipment. Because our cash flows from operations have been insufficient to fund all of these capital requirements, we have depended on the availability of financing under credit arrangements with third parties.

Our business strategy with regard to operations focuses on the following:

- maximizing performance at our existing facilities;
- focusing on profitable contracting;
- expanding MRI, CT and PET applications;
- optimizing operating efficiencies; and
- expanding our networks.

On April 6, 2010, we completed a series of transactions which we refer to as our "debt refinancing plan" for an aggregate of $585.0 million. As part of the debt refinancing plan, our wholly owned subsidiary Radnet Management, Inc. issued and sold $200.0 million in 10 3/8% senior notes due 2018 (the "senior notes"). All payments of the senior notes, including principal and interest, are guaranteed jointly and severally on a senior unsecured basis by RadNet, Inc. and all of Radnet Management’s current and future domestic wholly owned restricted subsidiaries. The senior notes were issued under an indenture, dated April 6, 2010, by and among Radnet Management, as issuer, RadNet, Inc., as parent guarantor, the subsidiary guarantors thereof and U.S. Bank National Association, as trustee, in a private placement that was not subject to the registration requirements of the Securities Act of 1933, as amended (the “Securities Act”). We subsequently exchanged the senior notes initially issued on April 6, 2010 in a private placement for publicly registered exchange notes with nearly identical terms. The exchange offer was completed on February 14, 2011.

In addition to the issuance of senior notes, Radnet Management entered into a new Credit and Guaranty Agreement with a syndicate of lenders (the "New Credit Agreement"), whereby Radnet Management obtained $385.0 million in senior secured first-lien bank financing, consisting of (i) a $285.0 million, six-year term loan facility and (ii) a $100.0 million, five-year revolving credit facility, including a swing line subfacility and a letter of credit subfacility (collectively, the “New Credit Facilities”). Radnet Management’s obligations under the New Credit Agreement are unconditionally guaranteed by RadNet, Inc., all of Radnet Management’s current and future wholly owned domestic subsidiaries as well as certain affiliates, including Beverly Radiology Medical Group III and its equity holders (Beverly Radiology Medical Group, Inc., BreastLink Medical Group, Inc. and ProNet Imaging Medical Group, Inc.). These New Credit Facilities created by the New Credit Agreement are secured by a perfected first-priority security interest in all of Radnet Management’s and the guarantors’ tangible and intangible assets, including, but not limited to, pledges of equity interests of Radnet Management and all of our current and future wholly owned domestic subsidiaries.

In connection with the issuance of the outstanding senior notes and entering into the New Credit Agreement, Radnet Management used the net proceeds from the issuance of the senior notes and the New Credit Facilities created by the New Credit Agreement to repay in full its existing first lien term loan for $242.0 million in aggregate principal amount outstanding, which would have matured on November 15, 2012, and its second lien term loan for $170.0 million in aggregate principal amount outstanding, which would have matured on November 15, 2013.

On November 8, 2011, in conjunction with our acquisition of the U.S. imaging operations of CML HealthCare Inc., we increased the size of our revolving credit facility by $21.25 million, to $121.25 million of total borrowing capacity. The increased facility size provides additional borrowing availability to fund further acquisitions and general working capital needs.

At June 30, 2012, we had $200.0 million aggregate principal amount of senior notes outstanding, $278.6 million of senior secured term loan debt outstanding and $59.5 million outstanding under our revolving credit facility. We had $61.75 million of available credit under our revolving credit facility, subject to borrowing conditions under that facility as further described in our annual report on Form 10-K for the fiscal year ended December 31, 2011. As of June 30, 2012, we were in compliance with all covenants under the New Credit Facilities and the senior notes.

NOTE 2 – FACILITY ACQUISITIONS

On May 1, 2012, we completed our acquisition of Advanced Medical Imaging of Stuart, L.P., which consists of two multi-modality imaging centers located in Stuart, Florida, for cash consideration of $1.0 million and the assumption of approximately $250,000 of unfavorable operating lease contracts. We have made a fair value determination of the acquired assets and assumed liabilities and approximately $39,000 of fixed assets, $88,000 of other current assets and $1.1 million of goodwill was recorded with respect to this transaction.

On April 1, 2012, we completed our acquisition of West Coast Radiology, which consists of five multi-modality imaging centers in Orange County, California, for cash consideration of $8.1 million and the assumption of approximately $1.4 million of capital lease obligations. The centers are located in Anaheim, Santa Ana/Tustin, Irvine and Mission Viejo/Laguna Niguel and operate a combination of MRI, CT, ultrasound, mammography, X-ray and other related modalities. We have made a fair value determination of the acquired assets and assumed liabilities and approximately $715,000 of working capital, $3.1 million of fixed assets, $5.4 million of goodwill, and $200,000 of intangible assets was recorded with respect to this transaction.

On February 29, 2012, we completed the acquisition of a multi-modality imaging center from TODIC, L.P. located in Camarillo, California for cash consideration of $350,000 and the assumption of a $121,000 capital lease liability. The facility provides MRI, CT, mammography, ultrasound and X-ray services. We have made a fair value determination of the acquired assets and assumed liabilities and approximately $425,000 of fixed assets and $86,000 of goodwill was recorded with respect to this transaction as well as the assumption of approximately $40,000 of accrued liabilities.

On February 29, 2012, we completed the acquisition of a multi-modality imaging center from Progressive MRI, LLC located in Frederick, Maryland for cash consideration of $230,000. The facility provides MRI, CT, mammography, ultrasound and X-ray services. We have made a fair value determination of the acquired assets and assumed liabilities and approximately $230,000 of fixed assets was recorded with respect to this transaction.

NOTE 3 – RECENT ACCOUNTING STANDARDS

In April 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2011-04, *Fair Value Measurement (Topic 820)* (“ASU 2011-04”), which contains amendments to achieve common fair value measurement and disclosures in U.S. GAAP and International Financial Reporting Standards. ASU 2011-04 explains how to measure fair value for financial reporting. The guidance does not require fair value measurements in addition to those already required or permitted by other Topics. This ASU was effective for the Company beginning January 1, 2012. The adoption of ASU 2011-04 did not have a material effect on the Company’s consolidated results of operations, financial position or liquidity.

On January 1, 2012, we adopted ASU 2011-05, “*Comprehensive Income (Topic 220): Presentation of Comprehensive Income,*” which updates existing guidance on comprehensive income. This guidance eliminates the option to present the components of other comprehensive income as part of our Condensed Consolidated Statements of Equity and Comprehensive Income, which was our previous presentation. It requires companies to present the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two statement approach which we have adopted, the first statement presents total net income and its components followed consecutively by a second statement that presents total other comprehensive income, the components of other comprehensive income and the total of comprehensive income. The adoption of this pronouncement did not have any effect on our financial condition or results of operations, though it did change our financial statement presentation.

On January 1, 2012, we adopted ASU 2011-07, "*Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*," which requires health care entities to present the provision for doubtful accounts relating to patient service revenue as a deduction from patient service revenue in the statement of operations rather than as an operating expense. Additional disclosures relating to sources of patient revenue and the allowance for doubtful accounts related to patient accounts receivable are also required. Such additional disclosures are included in Note 1. The adoption of this ASU had no impact on our financial condition, results of operations or cash flows, although it did change our financial statement presentation.

On January 1, 2012, we adopted ASU 2011-08, "*Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment*", simplifying how a company is required to test goodwill for impairment. Companies will now have the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the company determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary.

NOTE 4 – EARNINGS PER SHARE

Basic net income per share is based upon the weighted average number of shares of common stock outstanding during the periods presented, excluding non-vested restricted stock.

Diluted net income per share is based upon the weighted average number of shares of common stock, common equivalent stock and non-vested restricted stock outstanding during the periods presented.

The following table sets forth the computation of basic and diluted income loss per share (amounts in thousands, except share and per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income attributable to RadNet, Inc.'s common stockholders	$2,946	$3,521	$2,835	$2,645
BASIC INCOME PER SHARE ATTRIBUTABLE TO RADNET, INC.'S COMMON STOCKHOLDERS				
Weighted average number of common shares outstanding during the period	37,761,316	37,357,840	37,715,723	37,308,038
Basic income per share attributable to RadNet, Inc.'s common stockholders	$0.08	$0.09	$0.08	$0.07
DILUTED INCOME PER SHARE ATTRIBUTABLE TO RADNET, INC.'S COMMON STOCKHOLDERS				
Weighted average number of common shares outstanding during the period	37,761,316	37,357,840	37,715,723	37,308,038
Add nonvested restricted stock subject only to service vesting	521,667	–	494,744	–
Add additional shares issuable upon exercise of stock options and warrants	1,147,734	2,462,323	1,005,165	2,068,920
Weighted average number of common shares used in calculating diluted income per share	39,430,717	39,820,163	39,215,632	39,376,958
Diluted income per share attributable to RadNet, Inc.'s common stockholders	$0.07	$0.09	$0.07	$0.07

NOTE 5 – DERIVATIVE INSTRUMENTS

We are exposed to certain risks relating to our ongoing business operations. The primary risk managed by us using derivative instruments is interest rate risk. We have in the past entered into interest rate swap agreements to manage interest rate risk exposure. The interest rate swap agreements utilized by us effectively modified our exposure to interest rate risk by converting our floating-rate debt to a fixed rate basis during the period of the interest rate swap, thus reducing the impact of interest-rate changes on future interest expense.

At inception, we designated our interest rate swaps as cash flow hedges of floating-rate borrowings. In accordance with ASC Topic 815, derivatives that have been designated and qualify as cash flow hedging instruments are reported at fair value. The gain or loss on the effective portion of the hedge (i.e., change in fair value) is initially reported as a component of accumulated other comprehensive income in the consolidated statement of equity deficit. The remaining gain or loss, if any, is recognized currently in earnings. Unrealized gains or losses on the change in fair value of our interest rate swaps that do not qualify as hedges are recognized in earnings.

As a result of our refinancing and the New Credit Agreement and the issuance of the senior notes completed on April 6, 2010, our interest rate swaps do not match the terms of our current bank debt and so accordingly, we have determined that they are no longer designated as cash flow hedges. Accordingly, all changes in their fair value after April 6, 2010 are, and will continue to be recognized in earnings. As of April 6, 2010, the fair value of the interest rate swaps was a negative $10.4 million.

The related Accumulated Other Comprehensive Loss (“AOCL”) of $3.1 million associated with the negative fair values of these interest rate swaps on April 6, 2010, the date of our refinancing, is being amortized on a straight-line basis to interest expense through November 15, 2012, the maturity date of these cash flow hedges. From April 6, 2010 to June 30, 2012, approximately $2.7 million of AOCL was amortized to interest expense bringing the remaining balance of AOCL to approximately $367,000 at June 30 31, 2012.

At June 30, 2012 the negative fair value of these interest rate swaps was $2.3 million and was classified as accounts payable, accrued expenses and other in our consolidated balance sheet. For the three and six months ended June 30, 2012, we recognized approximately $1.5 million and $2.7 million, respectively, in other income related to the change in fair value of these interest rate swaps.

A tabular presentation of the fair value of derivative instruments as of June 30, 2012 is as follows (amounts in thousands):

Derivatives	**Balance Sheet Location**	Fair Value – Asset (Liability) Derivatives
Interest rate contracts	Accounts payable, accrued expenses and other	$ (2,336)

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A tabular presentation of the fair value of derivative instruments as of December 31, 2011 is as follows (amounts in thousands):

Derivatives	**Balance Sheet Location**	Fair Value – Asset (Liability) Derivatives
Interest rate contracts	Accounts payable, accrued expenses and other	$ (5,064)

A tabular presentation of the effect of derivative instruments on our statement of income is as follows (amounts in thousands):

For the Three Months Ended June 30, 2012

Ineffective Interest Rate Swap	Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Location of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)
Interest rate contracts	None	$1,515	Other income/ (expense)	* ($276)	Interest income/(expense)

For the Three Months Ended June 30, 2011

Ineffective Interest Rate Swap	Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Location of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)
Interest rate contracts	None	$690	Other income/ (expense)	* ($306)	Interest income/(expense)

For the Six Months Ended June 30, 2012

Ineffective Interest Rate Swap	Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Location of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)
Interest rate contracts	None	$2,728	Other income/ (expense)	* ($551)	Interest income/(expense)

For the Six Months Ended June 30, 2011

Ineffective Interest Rate Swap	Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Location of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)
Interest rate contracts	None	$2,060	Other income/ (expense)	* ($612)	Interest income/(expense)

* Amortization of OCI associated with the cash flow hedges through April 6, 2010 (see discussion above).

NOTE 6 – INVESTMENT IN JOINT VENTURES

We have eight unconsolidated joint ventures with ownership interests ranging from 35% to 50%. These joint ventures represent partnerships with hospitals, health systems or radiology practices and were formed for the purpose of owning and operating diagnostic imaging centers. Professional services at the joint venture diagnostic imaging centers are performed by contracted radiology practices or a radiology practice that participates in the joint venture. Our investment in these joint ventures is accounted for under the equity method. Investment in joint ventures increased approximately $793,000 to $23.1 million at June 30, 2012 compared to $22.3 million at December 31, 2011. This increase is primarily related to additional equity contributions made to one of these joint ventures of approximately $920,000 as well as our recording of equity earnings for the six months ended June 30, 2012 of approximately $3.2 million. Offsetting this increase is our respective share of distributions received during the six months ended June 30, 2012 of $3.4 million.

We received management service fees from the centers underlying these joint ventures of approximately $1.7 million for each of the three months ended June 30, 2012 and 2011, and approximately $3.4 million for each of the six months ended June 30, 2012 and 2011. We eliminate the portion of the fees earned associated with our ownership from our service revenue with an offsetting increase to our equity earnings.

The following table is a summary of key financial data for these joint ventures as of June 30, 2012 and for the six months ended June 30, 2012 and 2011 (in thousands):

Balance Sheet Data:	June 30, 2012
Current assets	$15,795
Noncurrent assets	36,909
Current liabilities	(7,221)
Noncurrent liabilities	(5,554)
Total net assets	$39,929
Book value of RadNet joint venture interests	$19,319
Cost in excess of book value of acquired joint venture interests	3,511
Elimination of intercompany profit remaining on RadNet's consolidated balance sheet	289
Total value of RadNet joint venture interests	$23,119
Total book value of other joint venture partner interests	$20,610

Income Statement Data for the six months ended June 30,	2012	2011
Net revenue	$41,955	$38,038
Net income	$7,016	$6,524

NOTE 7 – STOCK-BASED COMPENSATION

Options and Warrants

We have two long-term incentive plans that currently have outstanding stock options which we refer to as the 2000 Plan and the 2006 Plan. The 2000 Plan was terminated as to future grants when the 2006 Plan was approved by the stockholders in 2006. As of June 30, 2012, we have reserved for issuance under the 2006 Plan 11,000,000 shares of common stock. Certain options granted under the 2006 Plan to employees are intended to qualify as incentive stock options under existing tax regulations. In addition, we may issue non-qualified stock options and warrants under the 2006 Plan from time to time to non-employees, in connection with acquisitions and for other purposes and we may also issue stock under the 2006 Plan. Stock options and warrants generally vest over two to five years and expire five to ten years from date of grant.

As of June 30, 2012, 5,014,750, or approximately 80.5%, of the 6,231,250 outstanding stock options and warrants granted under our option plans are fully vested. During the six months ended June 30, 2012, we did not grant options or warrants under the 2006 Plan.

We have issued warrants outside the 2006 Plan under various types of arrangements to employees, and in exchange for outside services. All warrants issued to employees or consultants after our February 2007 listing on the NASDAQ Global Market have been characterized as awards under the 2006 Plan. All warrants outside the 2006 Plan have been issued with an exercise price equal to the fair value of the underlying common stock on the date of grant. The warrants expire from five to seven years from the date of grant. Vesting terms are determined by the board of directors or the compensation committee of the board of directors at the date of grant.

As of June 30, 2012, 1,502,898, or 100%, of all the outstanding warrants outside the 2006 Plan are fully vested. During the six months ended June 30, 2012, we did not grant warrants outside of our 2006 Plan.

The following summarizes all of our option and warrant transactions for the six months ended June 30, 2012:

Outstanding Options and Warrants Under the 2006 Plan and 2000 Plan	Shares	Weighted Average Exercise price Per Common Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Balance, December 31, 2011	6,656,250	$ 3.62		
Granted	–	–		
Exercised	–	–		
Canceled or expired	(425,000)	4.19		
Balance, June 30, 2012	6,231,250	3.58	2.39	$984,075
Exercisable at June 30, 2012	5,014,750	3.66	2.13	816,692

Non-Plan Outstanding Warrants	Shares	Weighted Average Exercise price Per Common Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Balance, December 31, 2011	2,502,898	$ 2.58		
Granted	–	–		
Exercised	(250,000)	2.52		
Canceled or expired	(750,000)	4.77		

Balance, June 30, 2012	1,502,898	1.50	1.15	$1,814,263
Exercisable at June 30, 2012	1,502,898	1.50	1.15	1,814,263

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (the difference between our closing stock price on June 30, 2012 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holder had all option holders exercised their options on June 30, 2012. The total intrinsic value of options and warrants exercised during the six months ended June 30, 2012 and 2011 was approximately $265,000 and $605,650, respectively. As of June 30, 2012, total unrecognized stock-based compensation expense related to non-vested employee awards was approximately $1.5 million, which is expected to be recognized over a weighted average period of approximately 1.6 years.

Restricted Stock Awards

The 2006 Plan permits the award of restricted stock. On January 3, 2012, we granted 525,000 restricted stock awards ("awards") to certain employees and 200,000 awards to non-employee directors of the Company. Of the awards granted, 241,667 were vested on the award date, 241,667 cliff vest after one year provided that the employees or non-employees remain continuously employed or engaged through the vesting date and 241,666 cliff vest after two years provided that the employees or non-employees remain continuously employed or engaged through the vesting date. We valued the awards based on the closing market price of our stock