ALLIANCE IMAGING INC /DE/
Form 10-Q
August 09, 2007

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: June 30, 2007

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 x No o

Indicate by check mark whether the registrant is a large accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer o Accelerated Filer x Non-accelerated filer 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 x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of July 31, 2007:

Common Stock, $.01 par value, 50,893,396 shares

ALLIANCE IMAGING, INC.
FORM 10-Q
June 30, 2007
Index

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALLIANCE IMAGING, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(in thousands)

	December 31, 2006	June 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 16,440	$ 36,507
Accounts receivable, net of allowance for doubtful accounts	51,569	57,096
Deferred income taxes	20,199	24,538
Prepaid expenses and other current assets	4,211	6,067
Other receivables	8,096	7,832
Total current assets	100,515	132,040
Equipment, at cost	769,967	772,482
Less accumulated depreciation	(425,790)	(432,877)
Equipment, net	344,177	339,605
Goodwill	150,069	150,069
Other intangible assets, net	35,782	33,384
Deferred financing costs, net	6,947	6,337
Other assets	27,036	17,159
Total assets	$ 664,526	$ 678,594
LIABILITIES AND STOCKHOLDERS DEFICIT		
Current liabilities:		
Accounts payable	$ 14,525	$ 11,768
Accrued compensation and related expenses	16,993	13,092
Accrued interest payable	4,320	4,419
Income taxes payable	637	
Other accrued liabilities	32,331	28,926
Current portion of long-term debt	2,858	3,042
Total current liabilities	71,664	61,247
Long-term debt, net of current portion	373,026	374,348
Senior subordinated notes	153,541	153,541
Minority interests and other liabilities	4,376	5,365
Deferred income taxes	78,893	87,691
Total liabilities	681,500	682,192
Commitments and contingencies (Note 10)		
Stockholders deficit:		
Common stock	499	503
Additional paid-in deficit	(7,070)	(3,616)
Accumulated comprehensive income	1,356	825
Accumulated deficit	(11,759)	(1,310)
Total stockholders deficit	(16,974)	(3,598)
Total liabilities and stockholders deficit	$ 664,526	$ 678,594

See accompanying notes.

ALLIANCE IMAGING, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME
(Unaudited)
(in thousands, except per share amounts)

	Quarter Ended June 30, 2006	2007	Six Months Ended June 30, 2006	2007
Revenues	$ 115,305	$ 111,756	$ 230,648	$ 221,162
Costs and expenses:				
Cost of revenues, excluding depreciation and amortization	62,593	58,152	122,460	114,329
Selling, general and administrative expenses	13,611	14,543	27,367	29,271
Severance and related costs	47	164	536	240
Depreciation expense	20,919	20,788	41,920	41,589
Amortization expense	1,229	1,194	2,473	2,404
Interest expense, net of interest income	10,022	10,388	19,796	20,462
Other (income) and expense, net	(256)	(211)	472	(531)
Total costs and expenses	108,165	105,018	215,024	207,764
Income before income taxes, minority interest expense, and earnings from unconsolidated investees	7,140	6,738	15,624	13,398
Income tax expense	3,556	3,241	7,207	7,193
Minority interest expense	495	471	1,035	992
Earnings from unconsolidated investees	(1,977)	(1,752)	(3,017)	(5,236)
Net income	$ 5,066	$ 4,778	$ 10,399	$ 10,449
Comprehensive income, net of taxes:				
Net income	$ 5,066	$ 4,778	$ 10,399	$ 10,449
Unrealized gain (loss) on hedging transactions, net of taxes	273	(262)	825	(531)
Comprehensive income	$ 5,339	$ 4,516	$ 11,224	$ 9,918
Earnings per common share:				
Basic	$ 0.10	$ 0.09	$ 0.21	$ 0.21
Diluted	$ 0.10	$ 0.09	$ 0.21	$ 0.20
Weighted average number of shares of common stock and common stock equivalents:				
Basic	49,758	50,462	49,684	50,210
Diluted	50,232	51,609	50,107	51,353

See accompanying notes.

4

ALLIANCE IMAGING, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(in thousands)

	Six Months Ended June 30, 2006	2007
Operating activities:		
Net income	$ 10,399	$ 10,449
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for doubtful accounts	1,593	2,334
Non-cash share-based compensation	1,308	1,845
Depreciation and amortization	44,393	43,993
Amortization of deferred financing costs	794	795
Adjustment of swaps to fair value	(494)	1,318
Distributions less than equity in undistributed income of investees	(188)	(469)
Deferred income taxes	6,552	5,361
Excess tax benefit from share-based payment arrangements		(567)
Loss (gain) on sale of assets	472	(531)
Changes in operating assets and liabilities:		
Accounts receivable	(6,903)	(7,861)
Prepaid expenses and other current assets	(1,312)	(1,856)
Other receivables	(2,091)	264
Other assets	(848)	(945)
Accounts payable	(8,915)	(3,470)
Accrued compensation and related expenses	1,866	(3,901)
Accrued interest payable	128	99
Income taxes payable	(11)	(637)
Other accrued liabilities	1,934	(3,389)
Minority interests and other liabilities	(259)	989
Net cash provided by operating activities	48,418	43,821
Investing activities:		
Equipment purchases	(43,035)	(34,935)
Decrease in deposits on equipment	10,388	9,814
Proceeds from sale of assets	2,322	1,978
Net cash used in investing activities	(30,325)	(23,143)
Financing activities:		
Principal payments on equipment debt	(1,934)	(1,550)
Proceeds from equipment debt		138
Principal payments on term loan facility	(2,675)	(600)
Principal payments on revolving loan facility	(28,825)	(7,000)
Proceeds from revolving loan facility	13,500	7,000
Payments of debt issuance costs	(186)	(185)
Proceeds from exercise of employee stock options	1,029	1,019
Excess tax benefit from share-based payment arrangements		567
Net cash used in financing activities	(19,091)	(611)
Net (decrease) increase in cash and cash equivalents	(998)	20,067
Cash and cash equivalents, beginning of period	13,421	16,440
Cash and cash equivalents, end of period	$ 12,423	$ 36,507
Supplemental disclosure of cash flow information:		
Interest paid	$ 19,676	$ 18,794
Income taxes paid, net of refunds	767	2,113
Supplemental disclosure of non-cash investing and financing activities:		
Net book value of assets exchanged	$ 5,439	$ 1,016
Capital lease obligations assumed for the purchase of equipment debt	1,839	3,518
Equipment debt transferred to unconsolidated investee	(2,772)	
Comprehensive income (loss) from hedging transactions, net of taxes	825	(531)

See accompanying notes.

ALLIANCE IMAGING, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2007

(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 and six-month periods ended June 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. 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, 2006.

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. The Company records minority interest expense related to its consolidated subsidiaries which are not wholly owned. Investments in non-consolidated investees are accounted for under the equity method. At June 30, 2006 and 2007, the Company had $2,065 and $713, respectively, in accounts payable related to deposits on equipment.

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. 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 now records in its consolidated statements of operations (i) compensation cost for options granted, modified, repurchased or cancelled on or after January 1, 2006 under the provisions of SFAS 123(R) and (ii) compensation cost 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 FAS123R-3, Transition Election to Accounting for the Tax Effects of Share-Based Payment Awards (FSP). The Company has elected to follow the alternative transition method as described in the FSP 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

On November 2, 1999, in connection with a series of transactions contemplated by an Agreement and Plan of Merger between Viewer Acquisition Corp and the Company 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 June 30, 2007, a total of 1,957,785 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. A portion of the options vest in equal increments over five years and a portion vest after eight years (subject to acceleration if certain financial performance targets are achieved). The Company settles stock option exercises with newly issued shares of common stock.

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 forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of compensation expense to be recognized in future periods. The Company records non-cash share-based compensation for stock options granted with exercise prices below the fair value of the Company s common stock at the date of grant and for certain stock options subject to amended performance targets under the 1999 Equity Plan, as discussed below.

The following weighted average assumptions were used in the estimated grant date fair value calculations for stock option awards:

	Six Months Ended June 30,	
	2006	**2007**
Risk free interest rate	4.55 %	4.74 %
Expected dividend yield	0.00 %	0.00 %
Expected stock price volatility	56.7 %	60.4 %
Average expected life (in years)	6.69	6.61

There were no stock options granted during the second quarters ended June 30, 2006 or 2007.

The expected stock price volatility rates are based on a blend of the historical volatility of the Company s common stock and peer implied volatility. The risk free interest rates are based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected life of the option or award. The average expected life represents the weighted average period of time that options or awards granted are expected to be outstanding, as calculated using the simplified method described in the Securities and Exchange Commission s Staff Accounting Bulletin No. 107.

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 June 30, 2007. 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.

Under the 1999 Equity Plan, a portion of the options granted are performance options. These options vest on the eighth anniversary of the grant date if the option holder is still an employee, but the vesting accelerates if the Company meets the operating performance targets specified in the option agreements. On June 20, 2001, the Company s compensation committee authorized the Company to amend the option agreements under its 1999 Equity Plan to reduce the performance targets for 1,899,600 performance options out of the 2,284,222 performance options outstanding. On May 18, 2004, the Company s compensation committee authorized the Company to make a second amendment to the option agreements under its 1999 Equity Plan to further reduce the performance targets for all of the 1,914,500 performance options outstanding. As a result of the amendment, if the Company achieves the reduced performance targets but does not achieve the original performance targets, and an option holder terminates employment prior to the eighth anniversary of the option grant date, the Company would be required to record a non-cash stock-based compensation charge equal to the amount by which the actual value of the shares subject to the performance option on the date of the amendment exceeded the option s exercise price.

The following table summarizes the Company s stock option activity:

	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2006	4,094,325	$ 5.93		
Granted	655,500	7.28		
Exercised	(321,180)	3.17		
Canceled	(483,035)	5.92		
Outstanding at June 30, 2007	3,945,610	$ 6.38	7.45	$ 13,124
Vested and expected to vest in the future at June 30, 2007	3,202,040	$ 6.31	7.13	$ 10,947
Exercisable at June 30, 2007	1,413,128	$ 5.95	5.75	$ 5,296

The weighted average grant-date fair value of options granted during the six months ended June 30, 2006 and 2007 was $2.58 per share and $4.57 per share, respectively. The total intrinsic value of options exercised during the quarters ended June 30, 2006 and 2007 was $298 and $820, respectively. The total intrinsic value of options exercised during the six months ended June 30, 2006 and 2007 was $389 and $1,488, respectively. The total cash received from employees as a result of stock option exercises was $759 and $463 for the quarters ended June 30, 2006 and 2007, respectively. The total cash received from employees as a result of stock option exercises was $1,029 and $1,019 for the six months ended June 30, 2006 and 2007, respectively.

The following table summarizes the Company s unvested stock option activity:

	Shares	Weighted Average Grant Date Fair Value
Unvested at December 31, 2006	2,830,441	$ 3.54
Granted	655,500	4.57
Vested	(547,309)	3.63
Canceled	(406,150)	3.26
Unvested at June 30, 2007	2,532,482	$ 3.79

At June 30, 2007, the total unrecognized fair value compensation cost related to unvested stock options granted to both employees and non-employees was $5,383, which is expected to be recognized over a remaining weighted-average period of 3.39 years. The valuation model applied in this calculation utilizes highly subjective assumptions that could potentially change over time, including the expected forfeiture rate and performance targets. Therefore the amount of unrecognized compensation expense noted above does not necessarily represent the value that will ultimately be realized by the Company in the statements of operations. The total fair value of shares vested during the quarter and six months ended June 30, 2006 was $167, and $1,024, respectively. The total fair value of shares vested during the quarter and six months ended June 30, 2007 was $45, and $1,986, respectively.

Restricted Stock Awards

The 1999 Equity Plan, as amended and restated, permits the award of restricted stock, restricted stock units, stock bonus awards and performance-based awards. During 2007, the Company granted 625,000 restricted stock awards (award) to certain employees of the Company, with an effective grant date of January 1, 2007. These awards cliff vest after three years, provided that the employee remains continuously employed through the issuance date. For the quarter and six months ended June 30, 2007 the Company recorded non-cash share-based compensation expense related to these grants of $252 and $498, respectively.

The following table summarizes the Company s unvested restricted stock activity:

	Shares	Weighted Average Grant Date Fair Value
Unvested at December 31, 2006		
Granted	625,000	$ 6.65
Vested		
Canceled		
Unvested at June 30, 2007	625,000	$ 6.65

At June 30, 2007, the total unrecognized fair value compensation cost related to restricted stock awards granted to employees was $2,533, which is expected to be recognized over a remaining weighted-average period of 2.51 years. The valuation model applied in this calculation utilizes highly subjective assumptions that could potentially change over time, including the expected forfeiture rate. Therefore the amount of unrecognized compensation expense noted above does not necessarily represent the value that will ultimately be realized by the Company in the statements of operations.

Stock Bonus Award

During 2006 and 2007, the Company granted stock bonus awards (award) to certain employees of the Company. On the issuance date, the Company shall issue a number of shares of the Company s common stock (shares), equal to the bonus award divided by the fair market value of the shares at that time, provided that the employee remains continuously employed through the issuance date. For the quarter and six months ended June 30, 2006, the Company recorded non-cash share based compensation expense related to these grants of $125 and $250, respectively. For the quarter and six months ended June 30, 2007 the Company recorded non-cash share based compensation expense related to these grants of $167 and $333, respectively.

At June 30, 2007, the total unrecognized fair value compensation cost related to the stock bonus awards granted to employees was $917, which is expected to be recognized over a remaining weighted-average period of 1.69 years. The valuation model applied in this calculation utilizes highly subjective assumptions that could potentially change over time, including the expected forfeiture rate. Therefore the amount of unrecognized compensation expense noted above does not necessarily represent the value that will ultimately be realized by the Company in the statements of operations.

3. Recent Accounting Pronouncements

Uncertainty in Income Taxes **In July 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, (FIN 48), an interpretation of FASB Statement No. 109, Accounting for Income Taxes, (FASB 109). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB 109. This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 was effective for fiscal years beginning after December 15, 2006. The cumulative effect, if any, of applying FIN 48 is to be reported as an adjustment to the opening balance of retained earnings in the year of adoption. The impact of the Company s reassessment of its tax positions in accordance with FIN 48 did not have a material effect on the results of operations, financial condition or liquidity. See further discussion of FIN 48 at Note 8.**

Fair Value Measurements **In September 2006, the FASB issued SFAS 157, Fair Value Measurements (SFAS 157), which enhances the existing guidance for measuring assets and liabilities using fair value. This statement provides a single definition of fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 emphasizes fair value as a market-based measurement instead of an entity-specific measurement. The statement sets out a fair value hierarchy with the highest priority being quoted prices in active markets. SFAS 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is currently evaluating the provisions of SFAS 157 and the impact on its consolidated financial position and results of operations. The Company will adopt SFAS 157 for the fiscal year beginning January 1, 2008.**

Fair Value Option for Financial Assets and Liabilities In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115 (SFAS 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with the Board s long-term measurement objectives for accounting for financial instruments. SFAS 159 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is currently evaluating the provisions of SFAS 159 and the impact on our consolidated financial position and results of operations. The Company will adopt SFAS 159 for the fiscal year beginning January 1, 2008.

4. Goodwill and Intangible Assets

Changes in the carrying amount of goodwill are as follows:

Balance at December 31, 2006	$	150,069
Additions to goodwill during the period		
Balance at June 30, 2007	$	150,069

Intangible assets consisted of the following:

	December 31, 2006 Gross Carrying Amount	Accumulated Amortization	Intangible Assets, net	June 30, 2007 Gross Carrying Amount	Accumulated Amortization	Intangible Assets, net
Amortizing intangible assets:						
Customer contracts	$ 51,063	$ (22,909)	$ 28,154	$ 51,063	$ (24,946)	$ 26,117
Other	7,175	(2,726)	4,449	6,910	(3,092)	3,818
Total amortizing intangible assets	$ 58,238	$ (25,635)	$ 32,603	$ 57,973	$ (28,038)	$ 29,935
Intangible assets not subject to amortization			$ 3,179			$ 3,449
Total other intangible assets			$ 35,782			$ 33,384

The Company reviews the recoverability of the carrying value of goodwill on an annual basis or more frequently when an event occurs or circumstances change to indicate an impairment of these assets has possibly occurred. Goodwill is allocated to the Company s various reporting units which represent the Company s geographical regions. The Company compares the fair value of the reporting unit to its carrying amount to determine if there is potential impairment.

Amortization expense for intangible assets subject to amortization was $1,229 and $1,194 for the quarters ended June 30, 2006 and 2007, respectively, and $2,473 and $2,404 for the six months ended June 30, 2006 and 2007, respectively. The intangible assets not subject to amortization represent certificate of needs and regulatory authority rights which have indefinite useful lives.

Estimated annual amortization expense for each of the fiscal years ending December 31, is presented below:

2007	$ 4,680
2008	4,467
2009	4,146
2010	4,077
2011	3,935

5. Other Accrued Liabilities

Other accrued liabilities consisted of the following:

	December 31, 2006	June 30, 2007
Accrued systems rental and maintenance costs	$ 2,596	$ 1,504
Accrued site rental fees	1,507	1,322
Accrued property and sales taxes payable	12,055	12,948
Accrued self-insurance expense	6,915	7,262
Other accrued expenses	9,258	5,890
Total	$ 32,331	$ 28,926

6. Long-Term Debt and Senior Subordinated Credit Facility

Long-term debt consisted of the following:

	December 31, 2006	June 30, 2007
Term loan facility	$ 367,200	$ 366,600
Senior subordinated notes	153,541	153,541
Equipment debt	8,684	10,790
Long-term debt, including current portion	529,425	530,931
Less current portion	2,858	3,042
Long-term debt	$ 526,567	$ 527,889

7. Derivatives

In 2004, the Company entered into interest rate swap agreements, with notional amounts of $56,813, $46,813 and $48,438 to manage the future cash interest payments associated with a portion of the Company s variable rate bank debt. These agreements are three years in length. Two of these agreements matured in the second quarter of 2007. One of these agreements will mature in the fourth quarter of 2007. As of June 30, 2006 and 2007, the fair value of the Company s interest rate swap agreements was $3,318 and $408, respectively. Under these arrangements, the Company receives three-month London Interbank Offered Rate (LIBOR) and pays a fixed rate of 3.15%, 3.89% and 3.69%, respectively. The net effect is to record interest expense at fixed rates of 5.65%, 6.39% and 6.19%, respectively, as the debt incurs interest based on three-month LIBOR plus 2.50%. For the quarter and six months ended June 30, 2006 the Company received net settlement amounts of $465 and $771, respectively. For the quarter and six months ended June 30, 2007, the Company received net settlement amounts of $314 and $1,017, respectively. Changes in the fair value of the swap agreements are recorded in interest expense each period, as these transactions do not qualify for hedge accounting treatment. For the quarter and six months ended June 30, 2006 the Company recognized a reduction to interest expense of $52 and $494, respectively, based on the change in the fair value of these instruments. For the quarter and six months ended June 30, 2007 the Company recognized interest expense of $647 and $1,318, respectively, based on the change in the fair value of these instruments. The Company will continue to record subsequent changes in the fair value of the swaps through interest expense.

In the first quarter of 2005, the Company entered into multiple interest rate collar agreements for its variable rate bank debt. The total underlying notional amount of the debt was $178,000. Under these arrangements the Company has purchased a cap on the interest rate of 4.00% and has sold a floor of 2.25%. The Company paid a net purchase price of $1,462 for these collars. These agreements are two and three years in length and mature at various dates between January 2007 and January 2008. As of June 30, 2006 and 2007, the fair value of the Company s interest rate collar agreements was $3,901 and $1,393, respectively. For the quarter and six month period ended June 30, 2006, the Company received a net settlement amount of $287 and $355, respectively. For the quarter and six month period ended June 30, 2007, the Company received a net settlement amount of $468 and $1,096, respectively. The Company has designated these collars as cash flow hedges of variable future cash flows associated with its long-term debt. For the quarters ended June 30, 2006 and 2007, the Company recognized $273 and ($262), net of tax, respectively, in comprehensive income (loss), based on the change in fair value of these instruments. For the six months ended June 30, 2006 and 2007, the Company recognized $825, and ($531), net of tax, respectively, based on the change in fair value of these instruments. The Company will record subsequent changes in the fair value of the collars through comprehensive income (loss) during the period these instruments are designated as hedges.

The Company accounts for derivative instruments and hedging activities in accordance with the provisions of SFAS 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133) and SFAS 138, Accounting for Certain Derivative Instruments and Hedging Activities (SFAS 138), an amendment of SFAS 133. On the date the Company enters into a derivative contract, management may designate the derivative as a hedge of the identified exposure. The Company formally documents all relationships between hedging instruments and hedged items, as well as the risk-management objective and strategy for undertaking various hedge transactions. In this documentation, the Company specifically identifies the firm commitment or forecasted transaction that has been designated as a hedged item and states how the hedging instrument is expected to hedge the risks related to the hedged item. The Company formally measures effectiveness of its hedging relationships, both at the hedge inception and on an ongoing basis, in accordance with its risk management policy. The Company would discontinue hedge accounting prospectively (i) if it is determined that the derivative is no longer effective in offsetting change in the cash flows of a hedged item, (ii) when the derivative expires or is sold, terminated or exercised, (iii) because it is probable that the forecasted transaction will not occur, (iv) because a hedged firm commitment no longer meets the definition of a firm commitment, or (v) if management determines that designation of the derivative as a hedge instrument is no longer appropriate. The Company s derivatives are recorded on the balance sheet at their fair value. For derivatives accounted for as cash flow hedges any unrealized gains or losses on fair value are included in comprehensive income, net of tax, assuming perfect effectiveness. Any ineffectiveness is recognized in earnings.

8. Income Taxes

For the quarter and six months ended June 30, 2007, the Company recorded a provision for income taxes of $3,241 and $7,193, or 40.4% and 40.8% of the Company s pretax income, respectively. For the quarter and six months ended June 30, 2006, the Company recorded a provision for income taxes of $3,556 and $7,207, or 41.2% and 40.9% of the Company s pretax income, respectively. The Company s effective tax rates were higher than the federal statutory rates primarily as a result of state income taxes.

FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB 109. This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 was effective for fiscal years beginning after December 15, 2006. The cumulative effect, if any, of applying FIN 48 is to be reported as an adjustment to the opening balance of retained earnings in the year of adoption. The impact of the Company s reassessment of its tax positions in accordance with FIN 48 did not have a material effect on the results of operations, financial condition or liquidity.

As of January 1, 2007, the Company provided a liability of $1,495 for unrecognized tax benefits related to various federal and state income tax matters. This entire amount would reduce the Company s effective income tax rate if recognized.

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. As of January 1, 2007, the Company had approximately $176 in accrued interest and penalties which is included as a component of the $1,495 unrecognized tax benefit noted above. The liability for the payment of interest and penalties did not materially change as of June 30, 2007.

Alliance Imaging, Inc. and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state tax jurisdictions. The Company is currently open to audit under the statute of limitations by the Internal Revenue Service for the years ending December 31, 2003 through 2006. The Company and its subsidiaries state income tax returns are open to audit under the statute of limitations for the years ending December 31, 2002 through 2006. The Company does not anticipate a significant change to the total amount of unrecognized tax benefits within the next 12 months.

9. Earnings Per Common Share

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

	Quarter Ended June 30, 2006	**Six Months Ended June 30,**