

Alliance HealthCare Services, Inc
Form 10-Q
August 03, 2017
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended: June 30, 2017

Commission File Number: 001-16609

ALLIANCE HEALTHCARE SERVICES, INC.

(Exact name of registrant as specified in its charter)

DELAWARE 33-0239910
(State or Other Jurisdiction of (IRS Employer
Incorporation or Organization) Identification Number)

18201 Von Karman Avenue

Suite 600

Irvine, California 92612

(Address of Principal Executive Office) (Zip Code)

(949) 242-5300

(Registrant's Telephone Number, including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date. As of July 24, 2017, there were 10,831,300 shares of common stock outstanding.

ALLIANCE HEALTHCARE SERVICES, INC.

FORM 10-Q

June 30, 2017

Index

	Page
<u>PART I—FINANCIAL INFORMATION</u>	1
<u>Item 1—Financial Statements:</u>	1
<u>Condensed Consolidated Balance Sheets as of June 30, 2017 (Unaudited) and December 31, 2016</u>	1
<u>Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for the Three and Six Months Ended June 30, 2017 and 2016 (Unaudited)</u>	2
<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2017 and 2016 (Unaudited)</u>	3
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	5
<u>Item 2—Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 3—Quantitative and Qualitative Disclosures about Market Risk</u>	40
<u>Item 4—Controls and Procedures</u>	40
<u>PART II—OTHER INFORMATION</u>	41
<u>Item 1—Legal Proceedings</u>	41
<u>Item 1A—Risk Factors</u>	41
<u>Item 6—Exhibits</u>	42
<u>SIGNATURES</u>	43

PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALLIANCE HEALTHCARE SERVICES, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except per share amounts)

	June 30, 2017 (unaudited)	December 31, 2016 (audited)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 22,653	\$ 22,241
Accounts receivable, net of allowance for doubtful accounts of \$4,022 in 2017 and \$4,008 in 2016	80,922	77,496
Prepaid expenses	8,823	9,568
Other current assets	4,456	3,853
Total current assets	116,854	113,158
Plant, property and equipment, net	205,058	204,814
Goodwill	120,773	119,130
Other intangible assets, net	193,060	198,977
Other assets	18,006	23,785
Total assets	\$ 653,751	\$ 659,864
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable	\$ 21,681	\$ 28,185
Accrued compensation and related expenses	20,247	24,895
Accrued interest payable	3,316	3,308
Current portion of long-term debt	33,270	17,298
Current portion of obligations under capital leases	4,125	3,354
Other accrued liabilities	34,681	29,323
Total current liabilities	117,320	106,363
Long-term debt, net of current portion	490,668	515,407
Obligations under capital leases, net of current portion	13,941	12,686
Deferred income taxes	27,966	25,818
Other liabilities	12,800	9,093
Total liabilities	662,695	669,367
Commitments and contingencies (Note 13)		
Stockholders' deficit:		
Preferred stock, \$0.01 par value; 1,000,000 shares authorized and no shares issued and outstanding	—	—
Common stock, \$0.01 par value; 100,000,000 shares authorized; 10,989,273 and 10,970,937 issued in 2017 and 2016, respectively; 10,831,300 and	110	110

Edgar Filing: Alliance HealthCare Services, Inc - Form 10-Q

10,812,964 outstanding in 2017 and 2016, respectively		
Treasury stock, at cost - 157,973 shares in 2017 and 2016	(3,138)	(3,138)
Additional paid-in capital	61,963	61,353
Accumulated comprehensive income	33	10
Accumulated deficit	(198,825)	(197,900)
Total stockholders' deficit attributable to Alliance HealthCare Services, Inc.	(139,857)	(139,565)
Noncontrolling interest	130,913	130,062
Total stockholders' deficit	(8,944)	(9,503)
Total liabilities and stockholders' deficit	\$ 653,751	\$ 659,864

See accompanying notes.

1

ALLIANCE HEALTHCARE SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

AND COMPREHENSIVE INCOME (LOSS)

(Unaudited)

(in thousands, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Revenues	\$ 137,261	\$ 125,317	\$ 267,197	\$ 249,041
Costs and expenses:				
Cost of revenues, excluding depreciation and amortization	78,154	69,939	153,203	140,853
Selling, general and administrative expenses	22,003	23,175	45,538	48,440
Transaction costs	152	431	314	848
Shareholder transaction costs	2,523	1,498	3,392	2,507
Severance and related costs	389	708	1,023	2,424
Impairment charges	1,085	—	1,085	—
Depreciation expense	13,783	13,730	27,856	26,778
Amortization expense	3,274	2,494	6,549	4,937
Interest expense, net	8,937	8,872	17,637	16,367
Other income, net	(394)	(3,546)	(877)	(4,334)
Total costs and expenses	129,906	117,301	255,720	238,820
Income before income taxes, earnings from unconsolidated investees, and noncontrolling interest	7,355	8,016	11,477	10,221
Income tax expense	2,379	2,221	2,376	1,275
Earnings from unconsolidated investees	(367)	(393)	(703)	(645)
Net income	5,343	6,188	9,804	9,591
Less: Net income attributable to noncontrolling interest	(5,654)	(3,729)	(10,729)	(8,322)
Net (loss) income attributable to Alliance HealthCare Services, Inc.	\$(311)	\$2,459	\$(925)	\$1,269
Comprehensive (loss) income, net of taxes:				
Net income	\$5,343	\$6,188	\$9,804	\$9,591
Unrealized (loss) gain on hedging transactions, net of taxes of \$0, \$0, \$0 and \$0	(19)	84	(6)	46
Reclassification adjustment for losses realized and included in net loss, net of taxes of \$0, \$0, \$0 and \$0	10	—	29	—
Total comprehensive income, net of taxes	5,334	6,272	9,827	9,637
Comprehensive income attributable to noncontrolling interest	(5,654)	(3,729)	(10,729)	(8,322)
Comprehensive (loss) income attributable to Alliance HealthCare Services, Inc.	\$(320)	\$2,543	\$(902)	\$1,315

(Loss) income per common share attributable to Alliance HealthCare

Services, Inc.:					
Basic		\$(0.03)	\$0.23	\$(0.08)	\$0.12
Diluted		\$(0.03)	\$0.23	\$(0.08)	\$0.12

Weighted average number of shares of common stock and common

stock equivalents:					
Basic		10,989	10,882	10,981	10,771
Diluted		10,989	10,893	10,981	10,796

See accompanying notes.

ALLIANCE HEALTHCARE SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)

	Six Months Ended June 30,	
	2017	2016
Operating activities:		
Net income	\$9,804	\$9,591
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for doubtful accounts	1,167	1,356
Share-based payment	684	1,780
Depreciation and amortization	34,405	31,715
Amortization of deferred financing costs	4,924	3,312
Accretion of discount on long-term debt	263	254
Adjustment of derivatives to fair value	(11)	(45)
Distributions from unconsolidated investees	523	752
Earnings from unconsolidated investees	(703)	(645)
Deferred income taxes	2,148	940
Gain on sale of assets, net	(664)	(169)
Impairment charges	1,085	—
Changes in fair value of contingent consideration related to acquisitions	150	(3,640)
Excess tax benefit from share-based payment arrangements	—	436
Changes in operating assets and liabilities, net of the effects of acquisitions:		
Accounts receivable	(4,054)	(1,389)
Prepaid expenses	851	(119)
Other current assets	(227)	674
Other assets	68	4,240
Accounts payable	(4,583)	2,578
Accrued compensation and related expenses	(4,708)	2,820
Accrued interest payable	8	(70)
Income taxes payable	50	(36)
Other accrued liabilities	8,281	3,614
Net cash provided by operating activities	49,461	57,949
Investing activities:		
Equipment purchases	(11,205)	(33,975)
Increase in deposits on equipment	(8,004)	(13,847)
Acquisitions, net of cash received	(2,022)	(6,659)
Proceeds from sale of assets	971	370
Net cash used in investing activities	(20,260)	(54,111)
Financing activities:		
Principal payments on equipment debt and capital lease obligations	(8,141)	(8,035)
Proceeds from equipment debt	2,154	4,809
Principal payments on term loan facility	(2,600)	(2,600)
Principal payments on revolving loan facility	(20,000)	(24,000)
Proceeds from revolving loan facility	13,500	21,000
Principal payment on note payable	(2,954)	—

Edgar Filing: Alliance HealthCare Services, Inc - Form 10-Q

Payments of debt issuance costs and deferred financing costs	(288)	(25,059)
Distributions to noncontrolling interest in subsidiaries	(11,351)	(11,703)
Contributions from noncontrolling interest in subsidiaries	985	—
Payments for employee share-based compensation payroll taxes	(74)	—
Excess tax benefit from share-based payment arrangements	—	(436)
Issuance of common stock	—	1
Proceeds from exercise of stock options	—	614
Settlement of contingent consideration related to acquisitions	(20)	(810)
Proceeds from shareholder transaction	—	28,630
Net cash used in financing activities	(28,789)	(17,589)
Net increase (decrease) in cash and cash equivalents	412	(13,751)
Cash and cash equivalents, beginning of period	22,241	38,070
Cash and cash equivalents, end of period	\$22,653	\$24,319

See accompanying notes.

3

ALLIANCE HEALTHCARE SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

(Unaudited)

(in thousands)

	Six Months Ended June 30,	
	2017	2016
Supplemental disclosure of cash flow information:		
Interest paid	\$12,561	\$12,957
Income taxes paid (refunded), net	47	(92)
Supplemental disclosure of non-cash investing and financing activities:		
Capital lease obligations related to the purchase of equipment	3,442	1,499
Changes in equipment purchases in accounts payable and accrued equipment	(1,446)	352
Note payable assumed in connection with acquisition	2,954	—
Noncontrolling interest assumed in connection with acquisitions	488	2,948
Fair value of contingent consideration related to acquisitions	—	420

See accompanying notes.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2017

(Unaudited)

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

Basis of Presentation The accompanying condensed consolidated financial statements have been prepared by Alliance HealthCare Services, Inc. (the “Company” or “Alliance”) in accordance with accounting principles generally accepted in the United States of America (“GAAP”) 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 GAAP 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 three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017. The accompanying 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, 2016.

For a complete summary of the Company’s significant accounting policies, refer to Note 2, “Summary of Significant Accounting Policies,” in Part IV, Item 15 of the Company’s 2016 Form 10-K, filed with the SEC on March 10, 2017. There have been no material changes to the Company’s significant accounting policies during the six months ended June 30, 2017.

Pending Transaction On April 10, 2017, the Company entered into an agreement and plan of merger (the “Merger Agreement”) by and among Tahoe Investment Group Co., Ltd., an entity organized under the laws of the People’s Republic of China (“Tahoe”), THAIHOT Investment Company Limited, an exempted company incorporated under the laws of the Cayman Islands and indirect wholly-owned subsidiary of Tahoe (“THAIHOT”), THAIHOT Investment Company US Limited, a Delaware corporation and indirect wholly-owned subsidiary of Tahoe (“Parent”) and Alliance Healthcare Services Merger Sub Limited, a Delaware corporation and wholly-owned subsidiary of Parent (“Sub” and together with Tahoe, THAIHOT and Parent, the “Purchaser Parties”) providing for the merger of Sub with and into Alliance (the “Merger”), with Alliance surviving the Merger as a wholly-owned subsidiary of Parent. Under the Merger Agreement, the Purchaser Parties will acquire all of the Company’s outstanding common stock that is not beneficially owned by the Purchaser Parties or owned by the Company as treasury shares for \$13.25 per share. The Merger is subject to approval by Alliance’s stockholders, including a non-waiveable condition requiring approval by the holders of a majority of the outstanding shares of Alliance common stock that are not beneficially owned by the Purchaser Parties or certain senior executive officers of the Company, as well as certain other customary closing conditions. The Company’s board of directors, acting on the unanimous recommendation of a special committee, comprised solely of independent and disinterested directors of the Company who are not affiliated with Tahoe or management of the Company (the “Special Committee”), approved the Merger Agreement and the transactions contemplated by the Merger Agreement and resolved to recommend that the Company’s stockholders adopt the Merger Agreement and the transactions contemplated by the Merger Agreement. The Special Committee exclusively negotiated the terms of the Merger Agreement with Tahoe, with the assistance of independent financial and legal advisors. The Company will

hold a meeting of stockholders for the purpose of voting on the adoption of the Merger Agreement on August 15, 2017. If completed, the Merger will result in the Company becoming a privately-held company and Alliance's common stock would no longer be listed on the NASDAQ.

At the effective time of the Merger, each issued and outstanding share of common stock, other than shares owned by Alliance as treasury stock, shares beneficially owned by the Purchaser Parties, and shares owned by holders of common stock who shall neither have voted in favor of the Merger nor consented thereto in writing and who shall have properly and validly perfected, and not effectively withdrawn or lost, their statutory appraisal rights under Delaware law (such shares of common stock "dissenting shares"), will be converted into the right to receive \$13.25 in cash per share, without interest and subject to any withholding taxes (the "Merger Consideration"). Under the terms of the Merger Agreement, each in-the-money stock option, whether or not exercisable or vested, will be converted into the right to receive the excess of the Merger Consideration over the option exercise price. Restricted stock units ("RSUs") that are not subject to accelerated vesting in accordance with their terms will be converted into the right to receive restricted cash awards equal to the Merger Consideration multiplied by the number of shares underlying the RSUs and shall continue to be subject to the same vesting and payment conditions and schedules applicable to such RSUs. The Purchaser Parties have informed Alliance that they intend to fund the payment of the aggregate Merger Consideration from cash on hand. The Merger is not subject to a financing condition.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

The Merger Agreement contains certain termination rights for both Alliance and Parent, and further provides that upon the termination of the Merger Agreement under certain circumstances, Alliance will be required to pay Parent an expense reimbursement amount equal to \$1.5 million in immediately available funds or Parent will be required to pay Alliance an expense reimbursement amount equal to \$4.5 million in immediately available funds (as applicable). Subject to certain limitations, either Alliance or Parent may terminate the Merger Agreement if the Merger is not consummated by December 15, 2017 (the “Termination Date”); provided that the Company may extend the Termination Date for a single additional 60-day period under certain circumstances.

In connection with the Merger, the Special Committee waived the standstill provisions of the Governance, Voting and Standstill Agreement, dated March 29, 2016, by and among Alliance, THAIHOT and Tahoe solely for the purpose of permitting the Purchaser Parties to enter into the Merger Agreement, perform the Purchaser Parties’ obligations thereunder, and consummate the contemplated transactions.

Upon closing of the Merger, Alliance is expected to remain headquartered in Southern California. Alliance’s executive management team is expected to remain in place. All of Alliance’s divisions within the United States are expected to continue unaffected.

Principles of Consolidation The accompanying condensed consolidated financial statements of the Company include the assets, liabilities, revenues and expenses of all subsidiaries over which the Company exercises control. Intercompany transactions have been eliminated. The Company evaluates participating rights in its assessment of control in determining consolidation of joint venture partners. The Company records noncontrolling interest related to its consolidated subsidiaries that are not wholly-owned. Investments in unconsolidated investees over which it exercises significant influence but does not control are accounted for under the equity method.

Use of Estimates The preparation of consolidated financial statements in conformity with GAAP 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. Recent Accounting Pronouncements

Revenue Recognition In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, “Revenue from Contracts with Customers (Topic 606),” to clarify and converge the revenue recognition principles under GAAP and International Financial Reporting Standards and to develop guidance that would streamline and enhance revenue recognition requirements while also providing a more robust framework for addressing revenue issues. ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry specific guidance. Key provisions of the ASU involve a 5-step model specific to recognizing revenue derived from customer contracts. In addition, ASU 2014-09 provides implementation guidance on several other important topics, including the accounting for certain revenue-related costs. The Company will be required to capitalize costs to acquire new contracts, whereas currently, the Company expenses those costs as incurred. In August 2015, the FASB issued an amendment to provide a one-year deferral of the effective date to annual reporting periods beginning on or

after December 15, 2017 for publicly traded business entities. Early adoption of the standard for annual reporting periods beginning on or after December 15, 2016 is permitted. As a publicly traded business entity, ASU 2014-09 will be effective for the Company beginning on January 1, 2018. The Company is currently working through an adoption plan, including identifying its revenue streams and completing a preliminary analysis of how it currently accounts for revenue transactions compared to the revenue accounting required under the new standard. The Company intends to complete its adoption plan in 2017. This plan will include a review of transactions supporting each revenue stream to determine the impact of accounting treatment under Accounting Standards Codification (“ASC”) 606, “Revenue from Contracts with Customers,” and the completion of a rollout plan for implementation of the new standard with affected functions in its organization. Because of the nature of the work that remains, at this time the Company is unable to reasonably estimate the impact of adoption on its consolidated financial statements.

6

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

Leases In February 2016, the FASB issued ASU 2016-02, “Leases,” to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The ASU supersedes the current guidance. The primary difference between current guidance and ASU 2016-02 is the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. ASU 2016-02 also requires an entity to separate the lease components from the non-lease components (for example, maintenance services or other activities that transfer a good or service to the customer) in a contract. Only the lease components must be accounted for in accordance with this guidance. ASU 2016-02 is effective for publicly traded business entities for annual reporting periods beginning after December 15, 2018, including interim reporting periods within that reporting period. Early adoption is permitted. ASU 2016-02 will be effective for the Company beginning on January 1, 2019. The Company is assessing the impact, if any, that the adoption of ASU 2016-02 may have on its consolidated financial statements.

Share-based Payments In March 2016, the FASB issued ASU 2016-09, “Compensation – Stock Compensation (Topic 718),” which simplifies several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. ASU 2016-09 is effective for publicly traded business entities for annual reporting periods beginning after December 15, 2016, including interim periods within those annual reporting periods. The Company adopted ASU 2016-09 on January 1, 2017. As required by the standard, \$0.2 million of tax deficiencies recognized on stock-based compensation expense were reflected in the Company’s condensed consolidated statements of operations and comprehensive income (loss) as a component of “Income tax expense” rather than “Additional paid-in capital” on a prospective basis during the six months ended June 30, 2017. At January 1, 2017, the Company had no previously unrecognized excess tax benefits, the cumulative effect of which would be required by the standard to be recorded as an adjustment to accumulated deficit. The Company also elected to prospectively apply the change in presentation of excess tax benefits wherein excess tax benefits recognized on stock-based compensation expense were classified as operating activities in our condensed consolidated statements of cash flows for the six months ended June 30, 2017. Presentation requirements for cash flows related to employee taxes paid for withheld shares had no impact to all periods presented as such cash flows have historically been presented as financing activities. Further, the Company did not elect an accounting policy change to record forfeitures as they occur and thus continues to estimate forfeitures at each period.

Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments In August 2016, the FASB issued ASU 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments,” which is intended to reduce diversity in the classification of transactions related to debt prepayment or debt extinguishment costs, zero-coupon debt instruments settlement, contingent consideration payments made after a business combination, insurance claims settlement and corporate-owned life insurance settlement, distributions from equity method investments and beneficial interests in securitization transactions. This guidance is effective for publicly traded business entities for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. Early adoption is permitted. ASU 2016-15 will be effective for the Company beginning on January 1, 2018. The Company is assessing the impact, if any, that the adoption of ASU 2016-15 may have on its consolidated financial statements.

Income Taxes In October 2016, the FASB issued ASU 2016-16, "Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory." This amendment is intended to improve accounting for the income tax consequences of intra-entity transfers of assets other than inventory. In accordance with this guidance, an entity should recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. The ASU will be effective for the Company beginning on January 1, 2018. Early adoption is permitted. The Company is assessing the impact, if any, that the adoption of ASU 2016-16 may have on its consolidated financial statements.

Statement of Cash Flows: Restricted Cash In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash," which provides amendments to current guidance to address the classifications and presentation of changes in restricted cash in the statement of cash flows. ASU 2016-18 will be effective for the Company beginning on January 1, 2018. Early adoption is permitted. The Company does not anticipate that the adoption of ASU 2016-18 will have a material impact on its consolidated financial statements.

7

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

Business Combinations In January 2017, the FASB issued ASU 2017-01, “Business Combinations (Topic 805): Clarifying the Definition of a Business,” which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. ASU 2017-01 is effective for fiscal years beginning after December 15, 2017, including interim periods within that year. The amendments in ASU 2017-01 should be applied prospectively on or after the effective date. Early adoption is permitted. ASU 2017-01 will be effective for the Company beginning on January 1, 2018. The Company is assessing the impact, if any, that the adoption of ASU 2017-01 may have on its consolidated financial statements.

Accounting Changes and Error Corrections In January 2017, the FASB issued ASU No. 2017-03, “Accounting Changes and Error Corrections (Topic 250) and Investments – Equity Method and Joint Ventures (Topic 323): Amendments to SEC Paragraphs Pursuant to Staff Announcements at the September 22, 2016 and November 17, 2016 EITF Meetings.” The new guidance is intended to provide clarity in relation to the disclosure of the impact that ASU 2014-09 and ASU 2016-02 will have on the Company’s financial statements when adopted. The effective date for this guidance is the same as the effective dates for ASU 2014-09 and ASU 2016-02. The Company is currently evaluating the effect that the adoption of ASU 2017-03 will have on its consolidated financial statements.

Intangibles – Goodwill and Other In January 2017, the FASB issued ASU 2017-04, “Intangibles – Goodwill and Other (Topic 350) – Simplifying the Test for Goodwill Impairment,” which eliminates the second step from the goodwill impairment test and instead requires an entity to recognize a goodwill impairment charge for the amount by which the goodwill carrying amount exceeds the reporting unit’s fair value. The amendments in ASU 2017-04 are effective for public business entities for annual or interim goodwill impairment tests in annual periods beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company early-adopted ASU 2017-04 on a prospective basis during the six months ended June 30, 2017. The adoption did not have any impact on the Company’s consolidated financial statements.

Share-based Payments – Modification Accounting In May 2017, the FASB issued ASU 2017-09, “Compensation – Stock Compensation (Topic 718): Scope of Modification Accounting,” which amends the scope of modification accounting for share-based payment arrangements and provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting. The amendments in ASU 2017-09 are effective for annual reporting periods, including interim periods within those annual reporting periods, beginning after December 15, 2017. Early adoption is permitted. ASU 2017-09 will be effective for the Company beginning on January 1, 2018. The Company’s adoption of ASU 2017-09 will not have a material impact on its consolidated financial statements.

3. Acquisitions and Transactions

Tahoe Transaction

On September 16, 2015, Tahoe agreed to purchase approximately 5,537,945 shares of the Company’s common stock from funds managed by Oaktree Capital Management, L.P. (“Oaktree”) and MTS Health Investors, LLC (“MTS”), and Larry C. Buckelew (together, the “Selling Stockholders”) for approximately \$102.5 million, or \$18.50 per share (the

“Tahoe Transaction”). In connection with the Tahoe Transaction, Tahoe and the Selling Stockholders agreed to bear a specified portion of the following Company expenses related to the Tahoe Transaction: (i) 100% of the fees and expenses incurred by the Company in connection with the amendment or waiver of its credit agreement, and (ii) all reasonable and documented fees and expenses incurred by the Company in connection with the Tahoe Transaction in excess of \$1.0 million. In addition, following approval of an authorized special committee of the board of directors, Tahoe funded a new management incentive arrangement which involved the issuance of \$1.5 million in cash-based awards to the Company’s management. The expenses associated with the cash-based awards were recognized by the Company over the required service period of the awards. The Company received reimbursements of \$15.3 million, which were net of taxes of \$0.2 million, prior to the Tahoe Transaction close from the Selling Stockholders. These reimbursements were accounted for as capital contributions from the Selling Stockholders. The Company accounted for reimbursements of \$13.5 million received subsequent to the Tahoe Transaction close from Tahoe as capital contributions. Costs that are a direct result of the Tahoe Transaction are included in “Shareholder transaction costs” in the Company’s consolidated statements of operations and comprehensive income (loss).

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

The Tahoe Transaction closed on March 29, 2016. Tahoe, through a wholly-owned subsidiary, owned an aggregate of approximately 51% of the Company's outstanding shares of common stock as of June 30, 2017. The Company has not agreed to pay any management fees to Tahoe for any financial advisory services provided to the Company.

On April 10, 2017, the Company entered into a Merger Agreement with Tahoe, pursuant to which Tahoe will acquire all of the Company's outstanding common stock that is not beneficially owned by Tahoe or owned by the Company as treasury shares. See Note 1 for details.

Pro Forma Impact of Acquisition

The following table provides pro forma revenues and results of operations as if the May 2016 acquisition of American Health Centers, Inc. had occurred at the beginning of the year prior to its acquisition date. The pro forma results were prepared from financial information obtained from the seller of the businesses, as well as information obtained during the due diligence process associated with the acquisition. The pro forma results reflect certain adjustments related to the acquisition, such as increased depreciation and amortization expense resulting from the stepped-up basis to fair value of assets acquired and adjustments to reflect the Company's borrowing and tax rates. The pro forma operating results do not include any anticipated synergies related to combining the businesses. Accordingly, such pro forma operating results were prepared for comparative purposes only and do not purport to be indicative of what would have occurred had the acquisition been made as of the beginning of the respective periods or of results that may occur in the future.

(in thousands, except per share amounts)	Three Months Ended June 30, 2016	Six Months Ended June 30, 2016
Revenues	\$125,496	\$249,856
Net income attributable to Alliance HealthCare Services, Inc.	2,533	1,612
Basic earnings per share	0.23	0.15
Diluted earnings per share	0.23	0.15

Restructuring Plan

From time to time, the Company's management implements individually immaterial restructuring plans, including the closure or consolidation of certain sites as a result of the loss of certain customers. The impact of the charges resulting from restructuring plans are summarized below:

(in thousands)	Three Months		Six Months	
	Ended		Ended	
	June 30,		June 30,	
	2017	2016	2017	2016
Cost of revenues, excluding depreciation and amortization	\$468	\$553	\$545	\$753
Selling, general and administrative expenses	74	567	93	598
Other expense, net	—	—	119	—
Total restructuring charges	\$542	\$1,120	\$757	\$1,351

The restructuring plans, under which costs were incurred during the three and six months ended June 30, 2017 and 2016, were adopted at varying times, beginning in 2009, and are expected to be completed by the first quarter of 2021.

4. Share-Based Payment

Stock Option Plans and Awards

In November 1999, the Company adopted an employee stock option plan (as amended and restated, the “1999 Equity Plan”) pursuant to which options and awards with respect to a total of 3,005,000 shares have become available for grant. As of June 30, 2017, a total of 995,439 shares remained available for grant under the 1999 Equity Plan.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

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

	Six Months Ended June 30, 2016	
Risk free interest rate	1.53	%
Expected dividend yield	—	%
Expected stock price volatility	66.5	%
Average expected life (in years)	6.0	
Weighted average fair value on grant date	\$ 4.32	

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

(dollars in thousands, except per share amounts)	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate
				Intrinsic Value ⁽¹⁾
Outstanding at December 31, 2016	650,969	\$ 18.51		
Canceled/forfeited	(43,980)	33.04		
Outstanding at June 30, 2017	606,989	\$ 17.46	6.2	\$ 2,067
Vested and expected to vest in the future at June 30, 2017	581,911	\$ 17.90	6.1	\$ 1,914
Vested and exercisable at June 30, 2017	485,752	\$ 20.02	5.5	\$ 1,326

(1) Represents the difference between the exercise price and the value of the Company's stock at fiscal quarter-end.

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

(dollars in thousands, except per share amounts)	Shares	Weighted Average	Aggregate Unrecognized Compensation	Weighted Average Period Over	Total Fair Value
--	--------	---------------------	---	------------------------------------	------------------------

	Grant Date	Fair Value	Which Expected to be Recognized (in years)
Unvested at December 31, 2016	187,804	\$ 4.33	
Vested	(62,303)	4.33	\$ 270
Forfeited	(4,264)	4.18	
Unvested at June 30, 2017	121,237	\$ 4.33	\$ 358 1.7

Stock Awards

The 1999 Equity Plan permits the award of restricted stock, RSUs, stock bonus awards and performance-based stock awards (collectively referred to as “stock awards”).

The following table summarizes the Company’s RSU activity:

	Shares	Weighted Average Grant Date	Weighted Average Aggregate Unrecognized Compensation	Period Over Which Expected to be Recognized (in years)
(dollars in thousands, except per share amounts)				
Unvested at December 31, 2016	167,853	\$ 8.37		
Vested	(25,690)	6.93		
Forfeited	(2,573)	6.93		
Unvested at June 30, 2017	139,590	\$ 8.66	\$ 668	0.9

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

Share-based Compensation Expense

The following table summarizes pre-tax share-based compensation expense included within “Selling, general and administrative expenses” in the condensed consolidated statements of operations and comprehensive income (loss):

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Share-based compensation expense	\$303	\$379	\$684	\$2,243 ⁽¹⁾

(1) Decrease in share-based compensation expense during the six months ended June 30, 2017, compared to the six months ended June 30, 2016, was primarily due to additional expense recognized related to a change in control in connection with the Tahoe Transaction in March 2016 (see Note 3). This includes cash paid of \$463 related to market performance RSUs, granted to executive management, which vested upon a change in control of the Company under the terms of the RSU award agreement.

5. Fair Value of Financial Instruments

Instruments Measured at Fair Value on a Recurring Basis

The following table summarizes the valuation of the Company’s financial instruments that are reported at fair value on a recurring basis:

(in thousands)	Fair Value as of June 30, 2017			Fair Value as of December 31, 2016				
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Financial assets:								
Interest rate contracts - asset position	\$52	\$ —	\$ 52	\$ —	\$55	\$ —	\$ 55	\$ —
Total financial assets	\$52	\$ —	\$ 52	\$ —	\$55	\$ —	\$ 55	\$ —
Financial liabilities:								

Contingent consideration related to												
acquisitions	\$685	\$	—	\$	—	\$685	\$555	\$	—	\$	—	\$555
Mandatorily redeemable noncontrolling												
interest	2,386	—	—	2,386	2,386	—	—	2,386				
Interest rate contracts - liability position	15	—	15	—	53	—	53	—				
Total financial liabilities	\$3,086	\$	—	\$	15	\$3,071	\$2,994	\$	—	\$	53	\$2,941

The Company's derivative instruments are primarily pay-fixed, receive-variable interest rate swaps based on the London interbank offered rate ("LIBOR") swap rate. The Company has elected to use the income approach to value these derivatives, using observable Level 2 market expectations at measurement date and standard valuation techniques to convert future amounts to a single present amount assuming that participants are motivated, but not compelled to transact. Level 2 inputs for interest rate swap valuations are limited to quoted prices for similar assets or liabilities in active markets (specifically futures contracts on LIBOR for the first two years) and inputs other than quoted prices that are observable for the asset or liability (specifically LIBOR cash and swap rates at commonly quoted intervals and implied volatilities for options). According to ASC 820, "Fair Value Measurement," the fair value measurement of an asset or liability must reflect the nonperformance risk of the entity and the counterparty. Therefore, the impact of the counterparty's creditworthiness and the Company's creditworthiness have also been factored into the fair value measurement of the derivative instruments. For additional information see Note 10.

The fair value of the liability for contingent consideration related to acquisitions was estimated using probability-adjusted performance estimates (Level 3 inputs) over the performance periods following the transaction dates. These estimates represent inputs for which market data are not available and are developed using the best information available about the assumptions that market participants would use when pricing the liability. Significant increases or decreases to either of these inputs in isolation would result in a significantly higher or lower liability. Ultimately, the liability will be equivalent to the amount paid, and the difference between the fair value estimate and amount paid will be recorded in earnings.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

Changes in the fair value of the Company's Level 3 liabilities for the six months ended June 30, 2017 were as follows:

(in thousands)	Contingent consideration related to acquisitions	Mandatorily redeemable noncontrolling interest
Balance at December 31, 2016	\$ 555	\$ 2,386
Fair value adjustment ⁽¹⁾	150	—
Settlement	(20)	—
Balance at June 30, 2017	\$ 685	\$ 2,386

(1) Adjustments to the estimated fair value of the contingent consideration are related to the actual versus expected performance of acquisitions and are included in "Other income, net" in the Company's consolidated statements of operations and comprehensive income (loss).

During the three and six months ended June 30, 2017, none of the Company's financial instruments were transferred from one level to another.

Instruments Not Recorded at Fair Value on a Recurring Basis

The following table summarizes the fair values and book values of the Company's long-term debt:

(in thousands)	June 30, 2017		December 31, 2016	
	Fair Value	Book Value	Fair Value	Book Value
Variable-rate debt	\$524,059	\$524,059	\$526,475	\$533,939
Fixed-rate debt	39,872	37,810	41,572	39,308
	\$563,931	\$561,869	\$568,047	\$573,247

The fair value of long-term debt is estimated using Level 2 inputs based on quoted market prices or pricing models using current market rates.

Assets and Liabilities Recorded at Fair Value on a Non-Recurring Basis

The Company also measures the fair value of certain assets on a non-recurring basis (utilizing Level 3 inputs), generally on an annual basis, in connection with acquisitions, or when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. These assets include goodwill, intangible assets, long-lived

assets and investments in unconsolidated investees. See Note 7 for a discussion of the Company's annual impairment test for goodwill and indefinite-lived intangible assets.

6. Impairment Charges

During the six months ended June 30, 2017, the Company reassessed its plans for the use of purchased software and determined it would not be able to utilize certain capabilities as planned. Accordingly, the Company recorded a non-cash charge to write down the asset by \$0.9 million in its Radiology Division.

During the six months ended June 30, 2017, the Company closed a site location and, as a result, recorded a non-cash charge to write off \$0.2 million of the remaining value of the physicians' referral network associated with that center in its Radiology Division.

There were no impairment charges during the six months ended June 30, 2016.

12

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

7. Goodwill and Intangible Assets

Changes in the carrying amount of goodwill are as follows:

(in thousands)	Radiology	Oncology	Interventional	Total
Balance at December 31, 2016	\$45,157	\$42,320	\$ 31,653	\$119,130
Goodwill acquired during the period ⁽¹⁾	—	1,643	—	1,643
Adjustments to goodwill during the period	—	—	—	—
Balance at June 30, 2017	\$45,157	\$43,963	\$ 31,653	\$120,773
Gross goodwill	\$199,499	\$63,865	\$ 31,653	\$295,017
Accumulated impairment charges	(154,342)	(19,902)	—	(174,244)
Balance at June 30, 2017	\$45,157	\$43,963	\$ 31,653	\$120,773

(1)The Company recorded goodwill related to an immaterial acquisition that occurred during the period. Intangible assets consisted of the following:

	Weighted Average Useful Life	June 30, 2017			December 31, 2016		
		Gross Carryover	Accumulated Amortization	Intangible Assets, Net	Gross Carryover	Accumulated Amortization	Intangible Assets, Net
(dollars in thousands)	(in years)	Amount	Amortization	Assets, Net	Amount	Amortization	Assets, Net
Finite-lived intangible assets:							
Customer contracts	16	\$230,208	\$(107,117)	\$123,091	\$230,323	\$(101,240)	\$129,083
Other	18	41,820	(22,816)	19,004	41,820	(22,141)	19,679
Total finite-lived intangible assets	16	\$272,028	\$(129,933)	\$142,095	\$272,143	\$(123,381)	\$148,762
Indefinite-lived intangible assets							
Total other intangible assets				50,965			50,215
				\$193,060			\$198,977

In 2017, the Company intends to perform its annual impairment test for goodwill and indefinite-lived intangible assets in the fourth quarter, absent other events occurring or changes in circumstances that would more-likely-than-not reduce the fair value of a reporting unit below its carrying amount. Based on financial information as of June 30, 2017, impairment testing was not required during the six months then ended.

Amortization expense for finite-lived intangible assets is reported as “Amortization expense” in the consolidated statements of operations and comprehensive income (loss). As of June 30, 2017, estimated future amortization expense for each of the fiscal years ending December 31, is presented below:

(in thousands)	
Remainder of 2017	\$6,594
2018	12,662
2019	12,173
2020	11,683
2021	10,774
Thereafter	88,209
	\$142,095

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

8. Supplemental Balance Sheet Information

Plant, property and equipment, net as of June 30, 2017 are as follows:

(in thousands)	Cost	Accumulated Depreciation	Net Carrying Amount
Furniture and fixtures	\$4,084	\$ (3,172)	\$912
Office equipment	82,808	(57,000)	25,808
Transportation and service equipment	15,681	(4,936)	10,745
Major equipment	767,219	(615,245)	151,974
Tenant improvements	43,627	(28,264)	15,363
Buildings and land	340	(84)	256
Total	\$913,759	\$ (708,701)	\$205,058

Plant, property and equipment, net as of December 31, 2016 are as follows:

(in thousands)	Cost	Accumulated Depreciation	Net Carrying Amount
Furniture and fixtures	\$4,905	\$ (4,231)	\$674
Office equipment	80,384	(57,295)	23,089
Transportation and service equipment	16,140	(4,291)	11,849
Major equipment	794,153	(639,452)	154,701
Tenant improvements	43,888	(29,665)	14,223
Buildings and land	340	(62)	278
Total	\$939,810	\$ (734,996)	\$204,814

Other accrued liabilities consisted of the following:

(in thousands)	June 30, 2017	December 31, 2016
Systems rental and maintenance costs	\$3,437	\$ 1,064
Site rental fees	901	899
Property and sales taxes payable	8,131	7,254
Self-insurance accrual	2,827	2,612
Legal fees	2,814	1,537
Deferred gain on sale of equipment	87	87
Equipment purchases	1,389	848

Edgar Filing: Alliance HealthCare Services, Inc - Form 10-Q

Customer overpayments	2,002	2,555
Contingent consideration related to acquisitions	685	555
Mandatorily redeemable noncontrolling interest	2,386	2,386
Other accrued liabilities	10,022	9,526
Total	\$34,681	\$ 29,323

14

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

9. Long-Term Debt and Senior Subordinated Credit Facility

Long-term debt consisted of the following:

	June 30,	December 31,
(in thousands)	2017	2016
Term loan facility	\$495,074	\$497,674
Discount on term loan facility	(1,047)	(1,310)
Revolving loan facility	15,000	21,500
Equipment under capital leases	18,066	16,040
Equipment debt	34,776	39,343
Deferred financing costs, net	(19,865)	(24,502)
Long-term debt, including current portion	542,004	548,745
Less current portion	(37,395)	(20,652)
Long-term debt	\$504,609	\$528,093

Equipment debt, collateralized by equipment, has interest rates ranging from 2.39% to 9.00% and is payable in various monthly principal and interest installments through 2021. Certain of the Company's equipment debt obligations are subject to covenants with which it must comply on a quarterly or annual basis. An amendment to the financing agreement with Bank of the West ("BOW") was executed on April 28, 2017, retroactive to March 31, 2017, that modified certain financial covenants. The Company was in compliance with all covenants as of June 30, 2017.

Capital leases, collateralized by equipment, have interest rates ranging from 2.68% to 6.23% and are payable in various monthly principal and interest installments through 2022.

Credit Facility and Senior Secured Term Loan Refinancing

On June 3, 2013, the Company replaced its existing credit facility with a new senior secured credit agreement with Credit Suisse AG, Cayman Islands Branch, as administrative agent, and the other lenders party thereto (the "Credit Agreement"). The Credit Agreement consists of (i) a \$340.0 million, six-year term loan facility, (ii) a \$50.0 million, five-year revolving loan facility, including a \$20.0 million sublimit for letters of credit, (iii) uncommitted incremental loan facilities of \$100.0 million of revolving or term loans, plus an additional amount if the Company's pro forma leverage ratio is less than or equal to 3.25, subject to receipt of lender commitments and satisfaction of specified conditions, and (iv) a \$80.0 million delayed draw term loan facility, which was drawn within thirty days of June 3, 2013 and used for the redemption of the Company's \$190.0 million of 8% Senior Notes ("Notes"). The delayed draw term loan facility converted into, and matched the terms of, the \$340.0 million term loan facility.

On October 11, 2013, the Company entered into an amendment to the Credit Agreement (the “First Amendment”). Pursuant to the First Amendment, the Company raised \$70.0 million in incremental term loan commitments to repurchase the remaining Notes. The Company used the proceeds from the incremental term loan commitments, borrowings under its revolving loan facility and cash on hand to complete the redemption of all its outstanding Notes on December 4, 2013.

On June 19, 2015, the Company entered into a second amendment to the Credit Agreement (the “Second Amendment”). Pursuant to the Second Amendment, the Company raised the remaining \$30.0 million in incremental term loan commitments. The funds were used to repay all outstanding borrowings under the Company’s revolving loan facility, to pay fees and expenses related to the Second Amendment, and for general corporate purposes. The incremental term loan under the Second Amendment was funded at 99.5% of the principal amount. Upon funding, the incremental term loans were converted to match all the terms of existing term loans.

On March 29, 2016, the Company entered into a third amendment to the Credit Agreement (the “Third Amendment”). Pursuant to the Third Amendment, (i) the defined term “Investors” was amended to include THAIHOT so that the sale by the Selling Stockholders would not be deemed to constitute a change of control, and (ii) the soft call provision was reinstated to commence on the date the Third Amendment is effective and end the date that is twelve months after such commencement.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

Under the soft call provision, which expired on March 29, 2017, if the Company made a voluntary prepayment of any term loan or prepaid, refinanced, substituted or replaced any term loan, and such action resulted in a reduction in the effective interest cost or weighted average yield of the term loan, then the Company should pay to the administrative agent, for the ratable account of each of the lenders holding term loans, a prepayment premium equal to 1.0% of the aggregate principal amount of the term loans so prepaid, refinanced, substituted or replaced.

In connection with the Third Amendment, the Company paid fees totaling \$25.0 million, which were capitalized and amortized using the effective interest method as interest expense over the term of the Credit Agreement. These fees were paid by both the buyer and sellers in the Tahoe Transaction.

Borrowings under the Credit Agreement bear interest through maturity at a variable rate based upon, at the Company's option, either the LIBOR or the base rate (which is the highest of the administrative agent's prime rate, one-half of 1.00% in excess of the overnight federal funds rate, and 1.00% in excess of the one-month LIBOR rate), plus, in each case, an applicable margin. With respect to the term loan facilities, the applicable margin for LIBOR loans is 3.25% per annum, and with respect to the revolving loan facility, the applicable margin for LIBOR loans ranges from 3.00% to 3.25% per annum, based on the applicable leverage ratio, and in each case, with a LIBOR floor of 1.00%. The applicable margin for base rate loans under the term loan facilities is 2.25% per annum and under the revolving loan facility ranges from 2.00% to 2.25% per annum, based on the applicable leverage ratio. The Company is required to pay a commitment fee which ranges from 0.38% to 0.50% per annum, based on the applicable leverage ratio, on the undrawn portion available under the revolving loan facility and variable per annum fees with respect to outstanding letters of credit.

The Company is required to make quarterly amortization payments on the term loan of \$1.3 million. The Company is also required to make mandatory prepayments of term loans under the Credit Agreement, subject to specified exceptions, from excess cash flow (as defined in the Credit Agreement) and with the proceeds of asset sales, debt issuances and specified other events.

As of June 30, 2017, the Company had \$30.4 million of available borrowings under the revolving loan facility, net of \$15.0 million outstanding on the revolving loan facility and \$4.6 million outstanding in letters of credit. The revolving loan facility matures on June 3, 2018.

Obligations under the Credit Agreement are guaranteed by substantially all the Company's direct and indirect domestic subsidiaries. The obligations under the Credit Agreement and the guarantees are secured by a lien on substantially all tangible and intangible property, and by a pledge of all of the shares of stock and limited liability company interests of the Company's direct and indirect domestic subsidiaries, of which the Company now owns or later acquires more than a 50% interest, subject to limited exceptions.

In addition to other covenants, the Credit Agreement places limits on the ability of the Company and its subsidiaries to declare dividends or redeem or repurchase capital stock; prepay, redeem or purchase debt; incur liens and engage in sale-leaseback transactions; make loans and investments; incur additional indebtedness; amend or otherwise alter debt and other material agreements; engage in mergers, acquisitions and asset sales; and transact with affiliates and alter

the business conducted by the Company and its subsidiaries.

The Credit Agreement also contains a leverage ratio covenant requiring the Company to maintain a maximum ratio of consolidated total debt to Consolidated Adjusted EBITDA, as defined in the Credit Agreement, that ranges from 4.95 to 1.00 to 4.30 to 1.00. At June 30, 2017, the Credit Agreement required a maximum leverage ratio of not more than 4.30 to 1.00. As of June 30, 2017, the Company's ratio of consolidated total debt to Consolidated Adjusted EBITDA calculated pursuant to the Credit Agreement was 3.95 to 1.00. Failure to comply with the covenants in the Credit Agreement could permit the lenders under the Credit Agreement to declare all amounts borrowed under the Credit Agreement, together with accrued interest and fees, to be immediately due and payable and to terminate all commitments under the Credit Agreement. As of June 30, 2017, the Company was in compliance with the covenants for the Credit Agreement.

16

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

Notes Payable and Line of Credit with PNC

The Company had notes payable to PNC Equipment Finance, LLC (“PNC”) totaling \$7.1 million at June 30, 2017. The notes payable are due in various installments through September 2021 at interest rates between 2.39% and 2.63% per annum. The notes are also collateralized by equipment and contain restrictive covenants. The Company also has a \$3.0 million line of credit with PNC, with interest calculated based on LIBOR plus 1.50%. As of June 30, 2017, there was \$2.1 million amount outstanding on the line of credit.

10. Derivatives

Interest Rate Cash Flow Hedges

The Company entered into multiple interest rate swap agreements to hedge the future cash interest payments on portions of its variable rate bank debt. As of June 30, 2017 and December 31, 2016, the Company had interest rate swap agreements to hedge approximately \$12.6 million and \$15.5 million of its variable rate bank debt, respectively, or 2.25% and 2.70% of total debt, respectively. The amount that the Company expects to reclassify from “Unrealized gain (loss) on hedging transactions, net of taxes” to “Interest expense, net” over the next twelve months is immaterial.

The Company’s interest rate cash flow hedges consist of:

(dollars in thousands)	Notional Amount	Fixed Payment Rate	Maturity Date	Fair Value	
				Asset (Liability) ⁽¹⁾ at June 30, 2017	December 31, 2016
Liability Derivatives					
Derivatives designated as cash flow hedging					
instruments:					
One-month LIBOR plus 2.50% interest rate swap,					
effective December 2012	\$ 560	3.75%	December 2017	\$ —	\$ (3)
One-month LIBOR plus 2.00% interest rate swap,					
effective March 2013	733	2.87%	April 2018	1	—

Edgar Filing: Alliance HealthCare Services, Inc - Form 10-Q

One-month LIBOR plus 2.00% interest rate swap,					
effective December 2015	4,196	3.69%	December 2021	(8)	(24)
One-month LIBOR interest rate swap, effective					
December 2015	1,023	1.37%	December 2020	3	—
One-month LIBOR interest rate swap, effective					
September 2016	3,971	1.17%	September 2021	38	33
Derivatives not designated as cash flow hedging					
instruments:					
One-month LIBOR interest rate swap			September 2017 -		
		0.75% -			
	1,302	1.68%	April 2020	2	(2)
One-month LIBOR interest rate swap, effective					
December 2014 ⁽²⁾	831	1.34%	November 2019	1	(2)
Total liability derivatives	\$ 12,616			\$ 37	\$ 2

- (1) The fair values of the interest rate swap asset and liabilities are included in “Other assets” and “Other accrued liabilities,” respectively, in the condensed consolidated balance sheets.
- (2) The interest rate swap agreement was de-designated as a cash flow hedge during the six months ended June 30, 2017.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

The following tables summarize the amounts of income (loss) recognized from derivative instruments for the periods indicated and the line items in the accompanying condensed consolidated statements of operations and comprehensive income (loss) where the results are recorded for cash flow hedges:

	Amount of (Loss) Gain		Location of Loss Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Loss		Location of Loss Recognized in Income on Derivatives	Amount of Loss Recognized	
	Three Months Ended June 30,	Three Months Ended June 30,		Three Months Ended June 30,	Three Months Ended June 30,		Three Months Ended June 30,	Three Months Ended June 30,
(in thousands)	2017	2016	(Effective Portion)	2017	2016	(Ineffective Portion)	2017	2016
Interest rate contracts	\$ (19)	\$ 6	Interest expense, net	\$ 10	\$ 140	Interest expense, net	\$ (2)	\$ —
Total	\$ (19)	\$ 6		\$ 10	\$ 140		\$ (2)	\$ —

	Amount of Loss		Location of Loss Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Loss		Location of Loss Recognized in Income on Derivatives	Amount of Loss Recognized	
	Six Months Ended June 30,	Six Months Ended June 30,		Six Months Ended June 30,	Six Months Ended June 30,		Six Months Ended June 30,	Six Months Ended June 30,
			(Effective Portion)			(Ineffective Portion)		

(in thousands)					June 30,	
	2017	2016	2017	2016	2017	2016
Interest rate contracts	\$ (6)	\$ (74)	\$ 29	\$ 223	\$ (2)	\$ (1)
Total	\$ (6)	\$ (74)	\$ 29	\$ 223	\$ (2)	\$ (1)

The effect of non-designated derivative instruments on the condensed consolidated statements of operations and comprehensive income (loss) for the three and six months ended June 30, 2017 and 2016 was immaterial.

11. Income Taxes

For the three and six months ended June 30, 2017, the Company recorded income tax expense of \$2.4 million and \$2.4 million, respectively, or 115.0% and 163.7%, respectively, of the Company's pre-tax income. For the three and six months ended June 30, 2016, the Company recorded an income tax expense of \$2.2 million and \$1.3 million, respectively, which were 47.4% and 50.1%, respectively, of the Company's pre-tax income. The provision (benefit) for income taxes for interim periods is determined using an estimate of the Company's annual effective tax rate, which is applied to current year-to-date pre-tax income (loss). Each quarter, the estimate of the annual effective tax rate is updated, and if the estimated effective tax rate changes, a cumulative adjustment is recorded. The Company's effective tax rate for the three and six months ended June 30, 2017 and 2016 differed from the federal statutory rate principally as a result of state income taxes and permanent non-deductible tax items, which include "Shareholder transaction costs," share-based payments, unrecognized tax benefits and other permanent differences. Pursuant to the Company's adoption of ASU 2016-09 on January 1, 2017, \$0.2 million of tax deficiencies recognized on stock-based compensation expense were reflected in the Company's condensed consolidated statements of operations and comprehensive income (loss) as a component of the "Income tax expense" rather than "Additional paid-in capital" on a prospective basis during the six months ended June 30, 2017. See Note 2 for details.

As of June 30, 2017 and December 31, 2016, the Company has provided a liability for \$0.3 of unrecognized tax benefits related to various federal and state income tax matters. The tax-effected amount that would reduce the Company's effective income tax rate if recognized is \$0.3 million and \$0.2 million as of June 30, 2017 and December 31, 2016, respectively.

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in "Income tax expense." Accrued interest and penalties related to unrecognized tax benefits as of June 30, 2017 and December 31, 2016 were not material.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

The Company is 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 ended December 31, 2013 through 2016. The Company's and its subsidiaries' state income tax returns are open to audit under the applicable statutes of limitations for the years ended December 31, 2012 through 2016. The Company does not anticipate a significant change to the total amount of unrecognized tax benefits within the next 12 months.

12. (Loss) Income Per Common Share

The following table sets forth the computation of basic and diluted net (loss) income per share:

(in thousands, except per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Numerator:				
Net (loss) income attributable to Alliance HealthCare Services,				
Inc.	\$(311)	\$2,459	\$(925)	\$1,269
Denominator:				
Weighted average shares — basic	10,989	10,882	10,981	10,771
Effect of dilutive securities:				
Stock options and RSUs	—	11	—	25
Weighted average shares — diluted	10,989	10,893	10,981	10,796
Net (loss) income per common share attributable to Alliance				
HealthCare Services, Inc.:				
Basic	\$(0.03)	\$0.23	\$(0.08)	\$0.12
Diluted	\$(0.03)	\$0.23	\$(0.08)	\$0.12
Stock options and RSUs excluded from the computation of diluted				
per share amounts:				
Weighted average shares for which the exercise price exceeds				
average market price of common stock ⁽¹⁾	N/A	776	N/A	478
Average exercise price per share that exceeds average market				
price of common stock ⁽¹⁾	N/A	\$17.89	N/A	\$24.79

(1)

The computation of diluted net loss per share for the three and six months ended June 30, 2017 excludes the effect of the potential exercise of all outstanding stock options and RSUs, because the Company had a net loss and inclusion would be anti-dilutive.

13. Commitments and Contingencies

Purchase Commitments

The Company has maintenance contracts with its equipment vendors and other service providers for substantially all of its radiology and oncology equipment. The contracts range from 1 to 5 years from inception and extend through the year 2021, but may be canceled by the Company under certain circumstances. The Company's total contract payments were \$11.7 million and \$10.0 million for the three months ended June 30, 2017 and 2016, respectively, and \$22.8 million and \$20.3 million for the six months ended June 30, 2017 and 2016, respectively. At June 30, 2017, the Company had binding equipment purchase commitments totaling \$19.0 million.

Guarantees and Indemnities

The Company has applied the disclosure provisions of ASC 460, "Guarantees," to its agreements that contain guarantee or indemnification clauses. These disclosure provisions expand those required by ASC 440, "Commitments," and ASC 450, "Contingencies," by requiring a guarantor to disclose certain types of guarantees, even if the likelihood of requiring the guarantor's performance is remote.

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

In the normal course of business, the Company has made certain guarantees and indemnities, under which it may be required to make payments to a guaranteed or indemnified party, in relation to certain transactions. The Company indemnifies other parties, including customers, lessors, and parties to other transactions with the Company, with respect to certain matters. The Company has agreed to hold the other party harmless against losses arising from certain events as defined within the particular contract, which may include, for example, litigation or claims arising from a breach of representations or covenants. In addition, the Company has entered into indemnification agreements with its executive officers and directors and the Company's bylaws contain similar indemnification obligations. Under these arrangements, the Company is obligated to indemnify, to the fullest extent permitted under applicable law, its current or former officers and directors for various amounts incurred with respect to actions, suits or proceedings in which they were made, or threatened to be made, a party as a result of acting as an officer or director.

It is not possible to determine the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Historically, payments made related to these indemnifications have been immaterial. At June 30, 2017, the Company has determined that no liability is necessary related to these guarantees and indemnities.

Litigation

In November 2015, the Company was served with a lawsuit in the United States District Court for the Northern District of Ohio by Todd S. Elwert, DC, Inc. The Complaint alleges violations of the Junk Fax Prevention Act for allegedly sending an unsolicited advertisement to Plaintiff which promoted commercial availability and/or quality of the Company's services. The Plaintiff further alleges that it is part of a class of similarly situated chiropractors who received the blast fax, and as such, requested class certification. The Company filed its response on December 17, 2015 and is currently in the discovery phase of the lawsuit. The Company intends to vigorously defend itself against the lawsuit and currently believes the ultimate disposition of these matters will not have a material adverse effect on its consolidated financial statements.

Other Matters

The Company is involved from time to time in routine litigation and regulatory matters incidental to the conduct of its business. The Company believes that resolution of such matters will not have a material adverse effect on its consolidated financial statements.

14. Related Party Transactions

Ownership Structure

On September 16, 2015, Tahoe agreed to purchase approximately 5,537,945 shares of the Company's common stock from funds managed by the Selling Stockholders. Tahoe, through a wholly-owned subsidiary, owned an aggregate of approximately 51% of the Company's outstanding shares of common stock as of June 30, 2017.

On April 10, 2017, the Company entered into a Merger Agreement with the Purchaser Parties, pursuant to which the Purchaser Parties will acquire all of the Company's outstanding common stock that is not beneficially owned by Tahoe or owned by the Company as treasury shares. See Note 1 for details.

Management Agreements

The Company had direct ownership in two unconsolidated investees at June 30, 2017 and December 31, 2016.

The following table summarizes revenues from management agreements with unconsolidated equity investees:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	2017	2016	2017	2016
Revenue from management agreements	\$307	\$352	\$781	\$705

20

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

The Company derives revenue from management agreements from services provided as part of its ongoing operations for and on behalf of the unconsolidated equity investees, which reimburse the Company for the actual amount of the expenses incurred. The Company records the expenses as “Cost of revenues, excluding depreciation and amortization” and the reimbursement as “Revenues” in its condensed consolidated statements of operations and comprehensive income (loss).

The following table summarizes the revenue and reimbursed expenses related to the Company’s unconsolidated equity investees:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	2017	2016	2017	2016
Revenue and reimbursed expenses	\$ 180	\$ 233	\$ 543	\$ 485

15. Investments in Unconsolidated Investees

The Company has direct ownership in two unconsolidated investees at June 30, 2017. The Company owns 15% and 50% of these investees, respectively, and provides management services under agreements with these investees, expiring at various dates through 2025. Both of these investees are accounted for under the equity method because the Company does not exercise control over the operations of these investees.

Set forth below are certain balance sheet data as of June 30, 2017 and December 31, 2016 and operating results for the three and six months ended June 30, 2017 and 2016 for the aggregate of the Company’s unconsolidated investees.

	June 30,	December 31,
(in thousands)	2017	2016
Balance sheet data:		
Current assets	\$4,017	\$ 2,860
Noncurrent assets	73	111
Current liabilities	681	760
Noncurrent liabilities	29	32

Edgar Filing: Alliance HealthCare Services, Inc - Form 10-Q

(in thousands)	Three Months		Six Months	
	Ended June 30, 2017	2016	Ended June 30, 2017	2016
Operating results:				
Revenues	\$2,833	\$2,662	\$5,426	\$4,963
Expenses	741	782	1,531	1,560
Net income	2,092	1,880	3,895	3,403
Earnings from unconsolidated investees	367	393	703	645

21

ALLIANCE HEALTHCARE SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

June 30, 2017

(Unaudited)

16. Stockholders' Deficit

The following table summarizes changes in the Company's consolidated stockholders' deficit, including noncontrolling interest, during the six months ended June 30, 2017.

	Common Stock		Treasury Stock		Paid-In Capital	Comprehensive Income	Accumulated Deficit	Stockholders' (Deficit) Equity		Total Stockholders' (Deficit) Equity
	Shares	Amount	Shares	Amount				Attributable to Alliance	Non-controlling Interest	
Balance at December 31, 2016	10,970,937	\$ 110	(157,973)	\$(3,138)	\$61,353	\$ 10	\$(197,900)	\$(139,565)	\$ 130,062	\$(9,503)
Vesting of stock awards, net	18,336	—	—	—	(74)	—	—	(74)	—	(74)
Share-based payment	—	—	—	—	684	—	—	684	—	684
Other comprehensive income	—	—	—	—	—	23	—	23	—	23
Noncontrolling interest assumed in connection with acquisition	—	—	—	—	—	—	—	—	488	488
Distributions to noncontrolling interest in subsidiaries	—	—	—	—	—	—	—	—	(11,351)	(11,351)

Contributions from noncontrolling interest in subsidiaries	—	—	—	—	—	—	—	—	985	985
Net (loss) income	—	—	—	—	—	—	(925)	(925)	10,729	9,804
Balance at June 30, 2017	10,989,273	\$ 110	(157,973)	\$(3,138)	\$61,963	\$33	\$(198,825)	\$(139,857)	\$130,913	\$(8,944)

The following table summarizes changes in the Company's consolidated stockholders' deficit, including noncontrolling interest, during the six months ended June 30, 2016.

	Common Stock		Treasury Stock		Paid-In Capital	Comprehensive Income (Loss)	Retained Earnings	Stockholders' (Deficit) Equity		Total Stockholders' (Deficit) Equity
	Shares	Amount	Shares	Amount				HealthCare Services, Inc	Non-controlling Interest	
Balance at December 31, 2015	10,774,857	\$ 108	(157,973)	\$(3,138)	\$29,297	\$(511)	\$(198,393)	\$(172,637)	\$95,017	\$(77,620)
Exercise of stock options	121,667	1	—	—	614	—	—	615	—	615
Shareholder transaction	—	—	—	—	28,629	—	—	28,629	—	28,629
Share-based payment	—	—	—	—	1,780	—	—	1,780	—	1,780
Share-based payment income tax benefit	—	—	—	—	315	—	—	315	—	315
Other comprehensive income	—	—	—	—	—	46	—	46	—	46
Net investments in subsidiaries	—	—	—	—	—	—	—	—	(8,754)	(8,754)
Net income	—	—	—	—	—	—	1,269	1,269	8,322	9,591
Balance at June 30, 2016	10,896,524	\$ 109	(157,973)	\$(3,138)	\$					