PRIMEDEX HEALTH SYSTEMS INC
Form 10-Q/A
October 02, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q/A

(AMENDMENT NO. 1)

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

For the quarterly period ended July 31, 2006

or

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

For the transition period from to

Commission File Number 0-19019

PRIMEDEX HEALTH SYSTEMS, INC.

(Exact name of registrant as specified in charter)

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

(310) 478-7808

(Registrant s telephone number, including area code)

n/a

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2).

Yes o No x

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY

PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes x No o

APPLICABLE ONLY TO CORPORATE ISSUERS:

The number of shares outstanding of the registrant s common stock as of September 6, 2006 was 42,228,761 (excluding treasury shares).

Explanatory Note: This Amendment No. 1 on Form 10-Q/A to our Quarterly Report on Form 10-Q for the fiscal quarter ended July 31, 2006 includes a new discussion in Item 2. under Overview with respect to our evaluation of disclosure controls and procedures, clarifies our discussion in Item 4., and adds a paragraph to our CEO and CFO certifications filed as Exhibits 31.1 and 31.2.

PART 1 FINANCIAL INFORMATION

Item 1. Financial Statements

PRIMEDEX HEALTH SYSTEMS, INC. AND AFFILIATES

CONSOLIDATED BALANCE SHEETS

	October 31, 2005	JULY 31, 2006 (Unaudited)
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 2,000	$ 2,000
Accounts receivable, net	22,319,000	24,299,000
Unbilled receivables and other receivables	476,000	1,035,000
Other	1,799,000	3,533,000
Total current assets	24,596,000	28,869,000
PROPERTY AND EQUIPMENT, NET	68,107,000	62,836,000
OTHER ASSETS		
Accounts receivable, net	1,267,000	1,379,000
Goodwill	23,099,000	23,099,000
Deferred financing costs	472,000	5,198,000
Trade name and other	3,692,000	5,219,000
Total other assets	28,530,000	34,895,000
Total assets	$ 121,233,000	$ 126,600,000
LIABILITIES AND STOCKHOLDERS DEFICIT		
CURRENT LIABILITIES		
Cash disbursements in transit	$ 3,425,000	$ 5,748,000
Line of credit	13,341,000	
Accounts payable and accrued expenses	22,469,000	20,962,000
Short-term notes expected to be refinanced:		
Notes payable	69,066,000	
Obligations under capital lease	56,927,000	
Notes payable	1,101,000	867,000
Obligations under capital lease	1,697,000	1,849,000
Total current liabilities	168,026,000	29,426,000
LONG-TERM LIABILITIES		
Subordinated debentures payable	16,147,000	16,147,000
Line of credit		6,868,000
Notes payable to related party	3,533,000	
Notes payable, net of current portion		145,154,000
Obligations under capital lease, net of current portion	4,129,000	3,552,000
Accrued expenses	31,000	22,000

Total long-term liabilities	23,840,000	171,743,000
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS DEFICIT	(70,633,000)	(74,569,000)
Total liabilities and stockholders deficit	$ 121,233,000	$ 126,600,000

The accompanying notes are an integral part of these financial statements

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PRIMEDEX HEALTH SYSTEMS, INC. AND AFFILIATES

CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

	THREE MONTHS ENDED		**NINE MONTHS ENDED**	
JULY 31,	**2005**	**2006**	**2005**	**2006**
NET REVENUE	$ 36,178,000	$ 40,336,000	$ 105,478,000	$ 118,462,000
OPERATING EXPENSES				
Operating expenses	26,790,000	30,105,000	79,792,000	88,701,000
Depreciation and amortization	4,243,000	4,071,000	12,905,000	12,175,000
Provision for bad debts	946,000	2,000,000	2,789,000	4,739,000
Loss on disposal of equipment, net		224,000	698,000	210,000
Total operating expenses	31,979,000	36,400,000	96,184,000	105,825,000
INCOME FROM OPERATIONS	4,199,000	3,936,000	9,294,000	12,637,000
OTHER EXPENSE (INCOME)				
Interest expense	4,278,000	5,392,000	12,788,000	14,386,000
Loss (gain) on debt extinguishment, net			(515,000)	2,097,000
Other income	(42,000)		(173,000)	
Other expense			25,000	788,000
Total other expense	4,236,000	5,392,000	12,125,000	17,271,000
LOSS BEFORE EQUITY IN INCOME OF INVESTEE	(37,000)	(1,456,000)	(2,831,000)	(4,634,000)
Equity in income of investee		61,000		61,000
NET LOSS	$ (37,000)	$ (1,395,000)	$ (2,831,000)	$ (4,573,000)
BASIC AND DILUTED NET LOSS PER SHARE	$	$ (.03)	$ (.07)	$ (.11)
WEIGHTED AVERAGE SHARES OUTSTANDING				
Basis and diluted	41,207,900	42,039,081	41,137,405	41,663,841

The accompanying notes are an integral part of these financial statements

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PRIMEDEX HEALTH SYSTEMS, INC. AND AFFILIATES

CONSOLIDATED STATEMENT OF STOCKHOLDERS DEFICIT

NINE MONTHS ENDED JULY 31, 2006

	Common Stock $.01 par value, 100,000,000 shares authorized		Paid-in	Treasury stock, at cost		Accumulated	Stockholders
	Shares	Amount	Capital	Shares	Amount	Deficit	Deficit
BALANCE OCTOBER 31, 2005	43,231,813	$ 433,000	$ 100,590,000	(1,825,000)	$ (695,000)	$ (170,961,000)	$ (70,633,000)
Issuance of warrant			110,000				110,000
Exercise of warrants	819,781	8,000	173,000				181,000
Exercise of options	2,167		1,000				1,000
Share-based payments			345,000				345,000
Net loss						(4,573,000)	(4,573,000)
BALANCE JULY 31, 2006 (UNAUDITED)	44,053,761	$ 441,000	$ 101,219,000	(1,825,000)	$ (695,000)	$ (175,534,000)	$ (74,569,000)

The accompanying notes are an integral part of these financial statements

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PRIMEDEX HEALTH SYSTEMS, INC. AND AFFILIATES

CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

NINE MONTHS ENDED JULY 31,	**2005**	**2006**
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 6,822,000	$ 4,633,000
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(2,831,000)	(6,041,000)
Investment in membership interest of PET center		(237,000)
Proceeds from sale of equipment	65,000	
Net cash used by investing activities	(2,766,000)	(6,278,000)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash disbursements in transit	1,254,000	2,323,000
Principal payments on notes and leases payable	(9,565,000)	(6,105,000)
Repayment of debt upon extinguishments		(141,242,000)
Proceeds from issuance of common stock		182,000
Proceeds from sale of equipment		15,000
Proceeds from borrowings upon refinancing		146,468,000
Proceeds from borrowings from related parties	1,370,000	
Debt issue costs		(5,608,000)
Payments on line of credit	(2,398,000)	
Proceeds from short and long-term borrowings on notes payable	5,284,000	5,612,000
Net cash provided (used) by financing activities	(4,055,000)	1,645,000
NET INCREASE (DECREASE) IN CASH	1,000	
CASH, beginning of period	1,000	2,000
CASH, end of period	$ 2,000	$ 2,000
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the period for interest	$ 12,241,000	$ 13,141,000

Supplemental Non-Cash Investing and Financing Activities

During the nine months ended July 31, 2006 and 2005, we entered into capital lease obligations for approximately $996,000 and $4,781,000, respectively.

The accompanying notes are an integral part of these financial statements

PRIMEDEX HEALTH SYSTEMS, INC. AND AFFILIATES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Nature of Business

Primedex Health Systems, Inc., or Primedex, incorporated on October 21, 1985, provides diagnostic imaging services in the state of California. Imaging services include magnetic resonance imaging, or MRI, computer tomography, or CT, positron emission tomography, or PET, nuclear medicine, mammography, ultrasound, diagnostic radiology, or X-ray, and fluoroscopy. Our operations comprise a single segment for financial reporting purposes.

The consolidated financial statements of Primedex include the accounts of Primedex, its wholly owned direct subsidiary, Radnet Management, Inc., or Radnet, and Beverly Radiology Medical Group III, or BRMG, which is a professional corporation, all collectively referred to as us or we . The consolidated financial statements also include Radnet Sub, Inc., Radnet Management I, Inc., Radnet Management II, Inc., SoCal MR Site Management, Inc., and Diagnostic Imaging Services, Inc., or DIS, all wholly owned subsidiaries of Radnet.

The operations of BRMG are consolidated with us as a result of the contractual and operational relationship among BRMG, Dr. Berger and us. We are considered to have a controlling financial interest in BRMG pursuant to the guidance in EITF 97-2. Medical services and supervision at most of our imaging centers are provided through BRMG and through other independent physicians and physician groups. BRMG is consolidated with Pronet Imaging Medical Group, Inc. and Beverly Radiology Medical Group, both of which are 99%-owned by Dr. Berger. Radnet provides non-medical, technical and administrative services to BRMG for which they receive a management fee.

Operating activities of subsidiary entities are included in the accompanying financial statements from the date of acquisition. All intercompany transactions and balances have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and, therefore, do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States for complete financial statements; however, in the opinion of our management, all adjustments consisting of normal recurring adjustments necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods ended July 31, 2006 and 2005 have been made. The results of operations for any interim period are not necessarily indicative of the results for a full year. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes thereto contained in our Annual Report on Form 10-K for the year ended October 31, 2005.

Liquidity and Capital Resources

We had a working capital deficit of $557,000 at July 31, 2006 compared to a $143.4 million deficit at October 31, 2005, and had losses from operations of $1.4 million and $4.6 million during the three and nine months ended July 31, 2006, respectively, and had losses from operations of $2.9 million for the nine months ended July 31, 2005. We also had a stockholders deficit of $74.6 million at July 31, 2006 compared to a $70.6 million deficit at October 31, 2005.

The working capital deficit increased as of October 31, 2005 due to the reclassification of approximately $109 million in notes and capital lease obligations as current liabilities expected to be refinanced. We were subject to financial covenants under our debt agreements and believed we may have been unable to continue to be in compliance with our existing financial covenants during fiscal 2006. As such, the associated debt was reclassified as a current liability.

Effective March 9, 2006, we completed the issuance of a $161 million senior secured credit facility that we used to refinance substantially all of our existing indebtedness (except for $16.1 million of outstanding subordinated debentures and approximately $5 million of capital lease obligations). We incurred fees and expenses for the transaction of approximately $5.6 million. Debt issue costs are being amortized on a straight-line basis over 65 months and are classified as Deferred financing costs. In addition, we recorded a net loss on extinguishments of debt of $2.1 million, which includes $1.2 million in pre-payment penalty fees that are unpaid as of July 31, 2006 and classified as accrued expenses under current liabilities. The facility provides for a $15 million five-year revolving credit facility, an $86 million term loan due in five years and a $60 million second lien term loan due in six years. The loans are subject to acceleration on December 27, 2007, unless we have made arrangements to discharge or extend our outstanding subordinated debentures by that date. We intend to retire the subordinated debentures prior to their due date of June 30, 2008. Under the terms and conditions of the new Second Lien Term Loan, subject to achieving certain leverage ratios, we have the right to raise up to $16.1 million in additional funds as part of the Second Lien Term Loan for the purposes of redeeming the subordinated debentures. Additionally, under the current facilities, we have the ability to pursue other funding sources to refinance the subordinated debentures. The loans are payable interest only monthly except for the $86 million term loan that requires amortization payments of 1.0% per annum, or $860,000, paid quarterly.

The revolving credit facility and the $86 million term loan bear interest at a base rate (base rate means corporate loans posted by at least 75% of the nation s 30 largest banks as quoted by the Wall Street Journal) plus 2.5%, or at our election, the LIBOR rate plus 4.0% per annum, payable monthly. The $60 million second lien term loan bears interest at the base rate plus 7.0%, or at our election, the LIBOR rate plus 8.5% per annum, payable monthly. The $86 million term loan includes amortization payments of 1.0% per annum, payable in quarterly installments of $215,000. Upon the close of the refinancing on March 9, 2006, we utilized approximately $1.5 million of the new $15 million revolving credit facility.

As part of the refinancing, we were required to swap at least 50% of the aggregate principal amount of the facilities to a floating rate within 90 days of the close of the agreement on March 9, 2006. On April 11, 2006, effective April 28, 2006, on $73.0 million (one half of our First and Second Lien Term Loans of $146.0 million), we entered into an interest rate swap fixing the LIBOR rate of interest at 5.47% for a period of three years. Previously, the interest rate on the $73.0 million was based upon a spread over LIBOR which floats with market conditions. In addition, as a requirement of the deal, 75% of our excess cash flow is to be used to repay principal on the $86 million term loan once per year within 105 days after our fiscal year end. Excess cash flow is defined as earnings before interest, taxes, depreciation and amortization plus decreases in working capital and extraordinary gains minus: (i) capital expenditures; (ii) interest expense; (iii) scheduled principal payments on existing debt; (iv) income taxes; (v) increases in working capital; (vi) extraordinary losses; (vii) voluntary prepayments of the $86 million term loan; (vii) and amounts paid for acquisitions.

Under the new facility, we are subject to various financial covenants including a limitation on capital expenditures, maximum days sales outstanding, minimum fixed charge coverage ratio, maximum leverage ratio and maximum senior leverage ratio. Availability under our $15 million revolving credit facility is governed by the margins calculated under the maximum senior leverage ratio and maximum total leverage ratio covenants. As of July 31, 2006, we had approximately $8.1 million of availability based upon our borrowing base formula.

During the second quarter of fiscal 2006, Howard G. Berger, M.D., our president, director and largest shareholder had outstanding advances to us of $2,605,000. Our obligation to Dr. Berger was repaid as part of our March 9, 2006 refinancing.

On July 6, 2006, Primedex entered into an agreement and plan of merger for the acquisition of Radiologix, Inc. by Primedex through the merger of a wholly-owned subsidiary of Primedex with and into Radiologix. Upon successful completion of the merger, Radiologix stockholders will receive a combination of cash and Primedex common stock in exchange for their shares of Radiologix common stock. Pursuant to the merger, Radiologix stockholders will receive aggregate consideration of 22,621,922 shares of Primedex common stock and $42,950,000 in cash. Based upon the August 17, 2006 closing price of Primedex common stock of $1.57, each Radiologix stockholder would receive $1.85 in cash for each Radiologix share, plus one share of Primedex common stock for total consideration valued at $3.42 per share. The merger agreement also provides Primedex the option to elect to reduce the share consideration by up to 3.5 million shares and to increase the cash consideration by $2 per share, provided that Primedex advises Radiologix of its election prior to the mailing of the proxy statement. Upon completion of the merger, we estimate that, subject to adjustment as described above, Radiologix s former stockholders will own approximately 34.9% of the then-outstanding shares of Primedex common stock, based on the number of shares of Radiologix and Primedex common stock outstanding on August 17, 2006. Primedex s stockholders will continue to own their existing shares. In connection with the proposals set forth in this joint proxy statement/prospectus, Primedex stock may be subject to transfer restrictions which are necessary to preserve Primedex s unrestricted use of its net operating loss carry-forwards.

Primedex has signed a commitment letter with GE Commercial Finance Healthcare Financial Services for a $405 million senior secured credit facility. The facility is expected to be used to finance the merger, to refinance existing indebtedness, to pay transaction costs and expenses relating to the merger and the credit facility and to provide financing for working capital needs post-merger. Consummation of the financing is a condition to the closing of the merger. The facility will consist of a revolving credit facility of up to $45 million, a $225 million term loan and a $135 million second lien term loan. The revolving credit facility will have a term of five years, the term loan will have a term of six years and the second lien term loan will have a term of six and one-half years. Interest is payable on all loans initially at an Index Rate plus the Applicable Index Margin, as defined. The Index Rate is initially a floating rate equal to the higher of the rate quoted from time to time by The Wall Street Journal as the base rate on corporate loans posted by at least 75% of the nation s largest 30 banks or the Federal Funds Rate plus 50 basis points. The Applicable Index Margin on each the revolving credit facility and the term loan is 2% and on the second lien term loan is 6%. Primedex may, after a certain period, request that the interest rate instead be based on LIBOR plus the Applicable LIBOR Margin, which is 3.5% for the revolving credit facility and the term loan and 7.5% for the second lien term loan. It is anticipated that the credit facility will include customary covenants for a facility of this type, including minimum fixed charge coverage ratio, maximum total leverage ratio, maximum senior leverage ratio, limitations on indebtedness, contingent obligations, liens, capital expenditures, lease obligations, mergers and acquisitions, asset sales, dividends and distributions, redemption or repurchase of equity interests, subordinated debt payments and modifications, loans and investments, transactions with affiliates, changes of control, and payment of consulting and management fees. The credit facility will contain such conditions to funding as are customary for senior secured facilities of this type.

We operate in a capital intensive, high fixed-cost industry that requires significant amounts of capital to fund operations. In addition to operations, we require significant amounts of capital for the initial start-up and development expense of new diagnostic imaging facilities, the acquisition of additional facilities and new diagnostic imaging equipment, and to service our existing debt and contractual obligations. Because our cash flows from operations have been insufficient to fund all of these capital requirements, we have depended on the availability of financing under credit arrangements with third parties. Historically, our principal sources of liquidity have been funds available for borrowing under our existing lines of credit, now with General Electric Capital Corporation. We finance the acquisition of equipment mainly through capital and operating leases.

As of July 31, 2006 and October 31, 2005, our line of credit liabilities were $6.9 million and $13.3 million, respectively.

The interim disclosures regarding liquidity and capital resources should be read in conjunction with the consolidated financial statements and related notes thereto contained in our Annual Report of Form 10-K for the year ended October 31, 2005.

Our business strategy with regard to operations will focus on the following:

- Maximizing performance at our existing facilities;
- Focusing on profitable contracting;
- Expanding MRI and CT applications
- Optimizing operating efficiencies; and
- Expanding our networks.

Our ability to generate sufficient cash flow from operations to make payments on our debt and other contractual obligations will depend on our future financial performance. A range of economic, competitive, regulatory, legislative and business factors, many of which are outside of our control, will affect our financial performance. Taking these factors into account, including our historical experience and our discussions with our lenders to date, although no assurance can be given, we believe that through implementing our strategic plans and continuing to restructure our financial obligations, we will obtain sufficient cash to satisfy our obligations as they become due in the next twelve months.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Revenue recognition Revenue consists of net patient fee for service revenue and revenue from capitation arrangements, or capitation revenue.

Net patient service revenue is recognized at the time services are provided net of contractual adjustments based on our evaluation of expected collections resulting from their analysis of current and past due accounts, past collection experience in relation to amounts billed and other relevant information. Contractual adjustments result from the differences between the rates charged for services performed and reimbursements by government-sponsored healthcare programs and insurance companies for such services.

Capitation revenue is recognized as revenue during the period in which we were obligated to provide services to plan enrollees under contracts with various health plans. Under these contracts, we receive a per enrollee amount each month covering all contracted services needed by the plan enrollees.

The following table summarizes net revenue for the three and nine months ended July 31, 2005 and 2006:

	Three Months Ended		**Nine Months Ended**	
	2005	**2006**	**2005**	**2006**
Net patient service	$ 26,544,000	$ 29,755,000	$ 77,670,000	$ 86,376,000
Capitation	9,634,000	10,581,000	27,808,000	32,086,000
Net revenue	$ 36,178,000	$ 40,336,000	$ 105,478,000	$ 118,462,000

Accounts receivable are primarily amounts due under fee-for-service contracts from third party payors, such as insurance companies and patients and government-sponsored healthcare programs geographically dispersed throughout California.

Accounts receivable as of October 31, 2005 are presented net of allowances of approximately $59,491,000, of which $56,296,000 is included in current and $3,195,000 is included in noncurrent. Accounts receivable as of July 31, 2006,

are presented net of allowances of approximately $54,397,000 of which $51,476,000 is included in current and $2,921,000 is included in noncurrent.

Credit risks Financial instruments that potentially subject us to credit risk are primarily cash equivalents and accounts receivable. We have placed our cash and cash equivalents with one major financial institution. At times, the cash in the financial institution is temporarily in excess of the amount insured by the Federal Deposit Insurance Corporation, or FDIC.

With respect to accounts receivable, we routinely assess the financial strength of our customers and third-party payors and, based upon factors surrounding their credit risk, establish a provision for bad debt. Net revenue by payor for the three and nine months ended July 31, 2005 and 2006 were:

	For the Three Months Ended				For the Nine Months Ended			
	2005		2006		2005		2006	
Capitation contracts	27	%	26	%	26	%	27	%
HMO/PPO/Managed care	22	%	24	%	22	%	24	%
Medicare	15	%	15	%	15	%	15	%
Blue Cross/Shield/Champus	14	%	14	%	14	%	15	%
Special group contract	9	%	8	%	9	%	8	%
Commercial insurance	4	%	3	%	4	%	3	%
Medi-Cal	3	%	4	%	3	%	3	%
Workers compensation	3	%	3	%	3	%	2	%
Other	3	%	3	%	4	%	3	%

Management believes that its accounts receivable credit risk exposure, beyond allowances that have been provided, is limited.

The Deficit Reduction Act of 2005 (DRA) was approved by Congress and signed into law on February 9, 2006. The DRA provides that reimbursement for the technical component for imaging services (excluding diagnostic and screening mammography) in non-hospital based freestanding facilities will be capped at the lesser of reimbursement under the Medicare Part B physician fee schedule or the Hospital Outpatient Prospective Payment System (HOPPS) schedule. Currently, the technical component of our imaging services is reimbursed under the Part B physician fee schedule, which for certain modalities like MRI and CT, allows for higher reimbursement on average than under the HOPPS. For other imaging exams, such as x-ray and ultrasound, reimbursement under the HOPPS is greater on average. Under the DRA, we will be reimbursed at the lower of the two schedules, beginning January 1, 2007.

The DRA also codifies the reduction in reimbursement for multiple images on contiguous body parts previously announced by the Centers for Medicare and Medicaid Services (CMS). In November 2005, CMS announced that it will pay 100% of the technical component of the higher priced imaging procedure and 50% for the technical component of each additional imaging procedure involving contiguous body parts when performed in the same session. Under current methodology, Medicare pays 100% of the technical component of each procedure. This rate reduction will occur in two steps, so that the reduction will be 25% for each additional imaging procedure in 2006 and another 25% in 2007. For the fiscal year ended October 31, 2005, Medicare revenue from our imaging centers represented approximately 15% of our total revenue. Of this amount, approximately 54% was from MRI and CT, the modalities affected more significantly by the reimbursement reductions. If both the HOPPS and contiguous body part reimbursement reductions contained in the DRA had been in effect during fiscal year 2005, we estimate that our revenue would have been reduced by approximately $4.5 million.

Significant Events On April 4, 2006, we settled a claim with Broadstream for $500,000. This claim arose in connection with a financing agreement we entered into with a third party. James Goldfarb, a partner of Broadstream Capital Partners, LLC (Broadstream), and once a member of our Board of Directors, arranged a meeting between us and a third party to discuss the third party financing the purchase of a portion of our debt owed to DVI Financial Services, which had filed for bankruptcy. Goldfarb alleged that, on behalf of Broadstream, he entered into an oral agreement with us under which we owed Broadstream a finder s fee for setting up this meeting. Broadstream filed suit against us, and Howard G. Berger, M.D., our president, for damages. Pursuant to the settlement, we agreed to pay to Broadstream $500,000 payable over a one and one-half year period.

We are engaged from time to time in the defense of lawsuits arising out of the ordinary course and conduct of our business. We believe that the outcome of our current litigation will not have a material adverse impact on our business, financial condition and results of operations. However, we could be subsequently named as a defendant in other lawsuits that could adversely affect us.

Reclassifications Certain prior year amounts have been reclassified to conform with the current period presentation. These changes have no effect on net income.

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NOTE 3 ACQUISITIONS AND DIVESTITURES

Acquisitions, openings and closings of imaging centers

In December 2005, we entered into a new building lease in Encino, California for approximately 10,425 square feet to begin the development of a new center, San Fernando Interventional Radiology and Imaging Center, which is expected to open by the end of this fiscal year. The center will offer MRI, CT, ultrasound and x-ray services as well as biopsy, angiography, shunt, and pain management procedures. The monthly rent is approximately $19,600 and the first month s rent will be due no later than September 2006.

Effective February 1, 2006, upon the inception of a new capitation arrangement, we opened two additional satellite offices in Yucaipa and Moreno Valley, California that provide x-ray services for our Riverside location. In addition, in February 2006, we opened one additional satellite office providing x-ray services in Temecula, California.

Effective February 1, 2006, we entered into a facility use agreement for an open MRI center in Vallejo, California. The agreement provides for the use of the equipment and facility for a monthly fee.

Effective February 1, 2006, we invested $237,000 for a 47.5% membership interest in an entity that operates a PET center in Palm Springs, California. We account for this investment under the equity method of accounting. Income in earnings of this equity method investment was approximately $61,000. The center will provide PET services for our existing facilities in the area replacing a prior arrangement where PET services were provided by a mobile unit for a per use fee. We have an option to purchase the other 52.5% interest subsequent to November 1, 2006 and prior to February 29, 2008 for $512,500.

On May 15, 2006, we opened an additional multi-modality site in Emeryville, California that provides MRI, CT and x-ray services. Ultrasound services will be added in the near future. We entered into a new building lease for 6,500 square feet with a beginning monthly rental of $9,754 and invested approximately $1.7 million in leasehold improvements for the new center. The improvements were paid for from working capital. Subsequent to the new center s opening, we decided to close our existing Emeryville MRI only facility and incurred a loss on the disposal of leasehold improvements in that center of approximately $143,000.

At various times, we may open or close small x-ray facilities acquired primarily to service larger capitation arrangements over a specific geographic region. Over time, patient volume from these contracts may vary, or we may end the arrangement, resulting in the subsequent closures of these smaller satellite facilities.

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NOTE 4 EQUITY BASED COMPENSATION

We have two long-term incentive stock option plans. The 1992 plan has not issued options since the inception of the new 2000 plan. The 2000 plan reserves 2,000,000 shares of common stock. Options granted under the plan are intended to qualify as incentive stock options under existing tax regulations. In addition, we have issued non-qualified stock options from time to time in connection with acquisitions and for other purposes and have also issued stock under the plan. Employee stock options generally vest over three years and expire five to ten years from date of grant. Of the 165,000 options granted under the plan during the nine months ended July 31, 2006, 150,000 options vested in full on the date of grant and 15,000 options vest over three years in equal installments beginning on the grant date. All 165,000 options are exercisable for period up to five years from the date of grant at a price equal to the fair market value of the common shares underlying the option at the date of grant. As of July 31, 2006, 807,500, or approximately 99%, of all the outstanding stock options are fully vested.

We have issued warrants under various types of arrangements to employees, in conjunction with debt financing and in exchange for outside services. All warrants are issued with an exercise price equal to the fair market value of the underlying common stock on the date of issuance. The warrants expire from five to seven years from the date of grant. Warrants issued to employees can vest immediately or up to seven years. The vesting terms are determined by the board of directors at the date of issuance. Of the 4,650,000 warrants granted during the nine months ended July 31, 2006, 700,000 vested in full on the date of grant and 3,950,000 vest in various stages beginning one year from the date of grant up to seven years. As of July 31, 2006, 6,189,000, or 56%, of all the outstanding warrants are fully vested.

During the first quarter of fiscal 2006, we adopted SFAS No. 123(R), Share-Based Payment, applying the modified prospective method. This Statement requires all equity-based payments to employees, including grants of employee options, to be recognized in the consolidated statement of earnings based on the grant date fair value of the award. Under the modified prospective method, we are required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. The fair values of all options were valued using a Black-Scholes model.

In anticipation of the adoption of SFAS No. 123(R), we did not modify the terms of any previously granted awards.

The compensation expense recognized for all equity-based awards is net of estimated forfeitures and is recognized over the awards service period. In accordance with Staff Accounting Bulletin (SAB) No. 107, we classified equity-based compensation within operating expenses with the same line item as the majority of the cash compensation paid to employees.

The following table illustrates the impact of equity-based compensation on reported amounts:

	For the Three Months Ended July 31, 2006(1)		For the Nine Months Ended July 31, 2006(1)	
	As Reported	Impact of Equity-Based Compensation	As Reported	Impact of Equity-Based Compensation
Income from operations (2)	$ 3,936,000	$ (108,000)	$ 12,637,000	$ (345,000)
Net loss	$ (1,395,000)	$ (108,000)	$ (4,573,000)	$ (345,000)
Net basic and diluted earning per share	$ (.03)	$	$ (.11)	$ (.01)

(1) Prior to the first quarter of fiscal 2006, we accounted for equity-based awards under the intrinsic value method, which followed the recognition and measurement principles of APB Opinion No. 25 and related Interpretations.

(2) The expense related includes $32,500 and $102,600 for the three and nine months ended July 31, 2006, respectively, for the unvested portion of previously granted employee awards outstanding as of the date of adoption.

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The following summarizes all of our option transactions from November 1, 2005 to July 31, 2006:

Outstanding Options	Shares	Weighted Average Exercise Price Per Common Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Balance, October 31, 2005	687,167	$ 0.51		
Granted	165,000	0.39		
Exercised	(2,167)	0.46		
Canceled or expired	(32,500)	0.41		
Balance, July 31, 2006	817,500	$ 0.49	4.14	$ 988,000
Exercisable at July 31, 2006	807,500	$ 0.49	4.08	$ 976,000

Outstanding Warrants	Shares	Weighted Average Exercise Price Per Common Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Balance, October 31, 2005	12,004,770	$ 0.60		
Granted	4,650,000	0.66		
Exercised	(1,319,781)	0.46		
Canceled or expired	(4,278,655)	0.64		
Balance, July 31, 2006	11,056,334	$ 0.63	3.80	$ 11,867,000
Exercisable at July 31, 2006	6,189,000	$ 0.61	2.32	$ 6,735,000

During the nine months ended July 31, 2006, there was a cashless exercise of 1,000,000 warrant shares for which 500,000 shares of common stock were issued.

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (the difference between our closing stock price on July 31, 2006 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holder had all option holders exercised their options on July 31, 2006. Total intrinsic value of options exercised during the nine months ended July 31, 2006 was approximately $1.0 million. As of July 31, 2006, total unrecognized share-based compensation expense related to non-vested employee awards was approximately $2.1 million, which is expected to be recognized over a weighted average period of approximately 7.0 years.

The weighted average fair value of options granted during the nine months ended July 31, 2006 was $0.49.

The fair value of each option granted is estimated on the grant date using the Black-Scholes option pricing model which takes into account as of the grant date the exercise price and expected term of the option, the current price of the underlying stock and its expected volatility, expected dividends on the stock and the risk-free interest rate for the term of the option. The following is the average of the data used to calculate the fair value:

June 31,	Risk-free interest rate	Expected term	Expected Volatility	Expected dividends
2005	3.00%	5 years	49.00%	
2006	4.73%	5 years	99.36%	

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We have determined the 2006 expected term assumption under the Simplified Method as defined in SAB 107. For fiscal 2006, expected stock price volatility is based on the historical volatility of our stock. The risk-free interest rate is based on the U.S. Treasury yield in effect at the time of grant with an equivalent remaining term. We have not paid dividends in the past and do not currently plan to pay any dividends in the near future.

Fair Value Disclosures Prior to Adopting SFAS No. 123(R)

We adopted SFAS 123(R) using the modified prospective transition method, which requires that application of the accounting standard as of November 1, 2005, the first day of our fiscal year 2006. Our consolidated financial statements as of and for the three and nine months ended July 31, 2006 reflect the impact of SFAS 123(R). In accordance with the modified prospective transition method, our consolidated financial statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS 123(R).

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition principles of SFAS No. 123 to stock-based employee compensation during fiscal 2005.

July 31,	Three Months Ended 2005	Nine Months Ended 2005
Net loss as reported	$ (37,000)	$ (2,831,000)
Deduct: Total stock-based employee compensation expense determined under fair value-based method	(94,000)	(186,000)
Pro forma net loss	$ (131,000)	$ (3,017,000)
Loss per share:		
Basic and diluted loss per share - as reported	$	$ (0.07)
Basic and diluted loss per share - pro forma	$	$ (0.07)

NOTE 5 CAPITAL TRANSACTIONS

On December 19, 2003, we issued a $1.0 million convertible subordinate note payable to Galt Financial, Ltd., at a stated rate of 11% per annum with interest payable quarterly. The note payable was convertible at the holder s option anytime after January 1, 2006 at $0.50 per share. As additional consideration for the financing, we issued a warrant for the purchase of 500,000 shares at an exercise price of $0.50 per share. We allocated $0.1 million to the value of the warrants. In November 2005, the right to convert the $1.0 million obligation into 2,000,000 shares of common stock was waived in exchange for the issuance of a five-year warrant to purchase 300,000 shares of our common stock at a price of $0.50 per share, the public market price on the date of the warrant, as consideration for the note being extended to July 1, 2006. We recorded $0.1 million for the estimated fair value of these warrants as a deferred cost which will be amortized as interest expense to the extended date of maturity. The note was repaid as part of our March 9, 2006 refinancing.

NOTE 6 SUBSEQUENT EVENTS

On August 25, 2006, we acquired the assets and business of Corona Imaging Center, in Corona, California, from an external third party for $1,500,000 financed through a third party lender over five years at 8.5%. In addition, we financed certain medical equipment for approximately $243,000 as part of the transaction. The center provides MRI, CT, ultrasound, and x-ray services. The center is 2,133 square feet with a monthly rental of approximately $3,839 per month with an initial lease term through November 2011. No goodwill is expected to be recorded in the transaction.

On September 1, 2006, effective September 5, 2006, we acquired the net assets and business of San Francisco Advanced Imaging Center, in San Francisco, California, from an external third party for $1,650,000 paid from working capital. The center provides MRI, CT and x-ray services. The center is 7,115 square feet with a monthly rental of approximately $29,000 with an initial lease term through April 2017. No goodwill is expected to be recorded in the transaction.

As of September 11, 2006, we were in the process of acquiring the assets and business of two additional facilities in Fresno, California and Irvine, California for an estimated $1,500,000 in cash and $500,000 in assumed liabilities, respectively. Both centers will offer MRI, CT, ultrasound and x-ray services and no goodwill is expected to be recorded in either transaction.

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Item 2: Management s Discussion and Analysis of Financial Condition and Results of Operations

Overview

As of July 31, 2006, we operate a group of regional networks comprised of 61 fixed-site freestanding outpatient diagnostic imaging facilities in California. We believe our group of regional networks is the largest of its kind in California. We have strategically organized our facilities into regional networks in markets, which have both high-density and expanding populations, as well as attractive payor diversity.

All of our facilities employ state-of-the-art equipment and technology in modern, patient-friendly settings. Many of our facilities within a particular region are interconnected and integrated through our advanced information technology system. Thirty four of our facilities are multi-modality sites, offering various combinations of MRI, CT, PET, nuclear medicine, ultrasound, X-ray and fluoroscopy services. Twenty-seven of our facilities are single-modality sites, offering either X-ray, MRI or PET services. Consistent with our regional network strategy, we locate our single-modality sites near multi-modality sites to help accommodate overflow in targeted demographic areas.

We derive substantially all of our revenue, directly or indirectly, from fees charged for the diagnostic imaging services performed at our facilities. During the nine months ended July 31, 2005 and 2006, we derived 61% and 58% of our net revenue, respectively, from MRI and CT scans. Over the past years, we have increased net revenue primarily through improvements in net reimbursement, expansions of existing facilities, upgrades in equipment and development of new facilities.

The fees charged for diagnostic imaging services performed at our facilities are paid by a diverse mix of payors, as illustrated for the nine months ended July 31, 2006 by the following table:

Payor Type	Percentage of Net Revenue	
Insurance(1)	41	%
Managed Care Capitated Payors	27	
Medicare/Medi-Cal	18	
Other2	10	
Workers Compensation/Personal Injury	4	

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(1) Includes Blue Cross/Blue Shield, which represented 15% of our net revenue for the nine months ended July 31, 2006.

(2) Includes co-payments, direct patient payments and payments through contracts with physician groups and other non-insurance company payors.

Our eligibility to provide service in response to a referral often depends on the existence of a contractual arrangement between the radiologists providing the professional medical services or us and the referred patient s insurance carrier or managed care organization. These contracts typically describe the negotiated fees to be paid by each payor for the diagnostic imaging services we provide. With the exception of Blue Cross/Blue Shield and government payors, no single payor accounted for more than 5% of our net revenue for the nine months ended July 31, 2006. Under our capitation agreements, we receive from the payor a pre-determined amount per member, per month. If we do not successfully manage the utilization of our services under these agreements, we could incur unanticipated costs not offset by additional revenue, which would reduce our operating margins.

The principal components of our fixed operating expenses, excluding depreciation, include professional fees paid to radiologists, except for those radiologists who are paid based on a percentage of revenue, compensation paid to technologists and other employees, and expenses related to equipment rental and purchases, real estate leases and insurance, including errors and omissions, malpractice, general liability, workers compensation and employee medical. The principal components of our variable operating expenses include expenses related to equipment maintenance, medical supplies, marketing, business development and corporate overhead. Because a majority of our expenses are fixed, increased revenue as a result of higher scan volumes per system can significantly improve our margins, while lower scan volumes can result in significantly lower margins.

BRMG strives to maintain qualified radiologists and technologists while minimizing turnover and salary increases and avoiding the use of outside staffing agencies, which are considerably more expensive and less efficient. In recent years, there has been a shortage of qualified radiologists and technologists in some of the regional markets we serve. As turnover occurs, competition in recruiting radiologists and technologists may make it difficult for our contracted radiology practices to maintain adequate levels of radiologists and technologists without

the use of outside staffing agencies. At times, this has resulted in increased costs for us.

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As part of our evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the fiscal year ended October 31, 2005, we concluded that we had insufficient personnel resources and technical accounting expertise within the accounting function to resolve the following non-routine or complex accounting matters: the recording of non-typical cost-based investments and unusual debt-related transactions and the appropriate analysis of the amortization lives of leasehold improvements in accordance with GAAP. We are committed to establish the necessary environment to ensure the effectiveness of these controls in the future and quality financial reporting. We experienced no impact on our financial statements for the year ended October 31, 2005 or for the nine months ended July 31, 2006 as a result of the ineffective controls over non-routine matters.

Adoption of SFAS No. 123(R) and Equity-Based Compensation Expense

During the first quarter of fiscal 2006, we adopted SFAS No. 123 (R), Share-Based Payment, applying the modified prospective method. This Statement requires all equity-based payments to employees, including grants of employee options, to be recognized in the consolidated statement of earnings based on the grant date fair value of the award. Under the modified prospective method, we are required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. The fair values of all options were valued using a Black-Scholes model.

In anticipation of the adoption of SFAS No. 123(R), we did not modify the terms of any previously granted awards.

Our operating earnings for the three and nine months ended July 31, 2006 were adversely affected by the impact of equity-based compensation due to the implementation of SFAS No. 123 (R). We recorded $108,000 and $345,000, respectively, for equity-based compensation during the three and nine months ended July 31, 2006. As of July 31, 2006, total unrecognized share-based compensation expense related to non-vested employee awards was approximately $2.1 million, which is expected to be recognized over a weighted-average period of approximately 7.0 years. The weighted fair value of options granted during the nine months ended July 31, 2006 was $0.49.

Our Relationship with BRMG

Howard G. Berger, M.D. is our President and Chief Executive, a member of our Board of Directors, and owns approximately 30% of Primedex s outstanding common stock. Dr. Berger also owns, indirectly, 99% of the equity interests in BRMG. BRMG provides all of the professional medical services at 46 of our facilities under a management agreement with us, and contracts with various other independent physicians and physician groups to provide all of the professional medical services at most of our other facilities. We obtain professional medical services from BRMG, rather than providing such services directly or through subsidiaries, in order to comply with California s prohibition against the corporate practice of medicine. However, as a result of our close relationship with Dr. Berger and BRMG, we believe that we are able to better ensure that professional medical services are provided at our facilities in a manner consistent with our needs and expectations and those of our referring physicians, patients and payors than if we obtained these services from unaffiliated practice groups.

Under our management agreement with BRMG, which expires on January 1, 2014, BRMG pays us, as compensation for the use of our facilities and equipment and for our services, a percentage of the gross amounts collected for the professional services it renders. The percentage, which was 79% at July 31, 2006, is adjusted annually, if necessary, to ensure that the parties receive fair value for the services they render. In operation and historically, the annual revenue of BRMG from all sources closely approximates its expenses, including Dr. Berger s compensation, fees payable to us and amounts payable to third parties. For administrative convenience and in order to avoid inconveniencing and confusing our payors, a single bill is prepared for both the professional medical services provided by the radiologists and our non-medical, or technical, services, generating a receivable for BRMG. Historically, BRMG financed these receivables under a working capital facility with Bridge Healthcare Finance LLC, or Bridge, and regularly advanced to us the funds that it drew under this working capital facility, which we used for our own working capital purposes. We repaid or offset these advances with periodic payments from BRMG to us under the management agreement. We guaranteed BRMG s obligations under this working capital facility. Effective March 9, 2006, the line of credit with Bridge was paid and closed with the issuance of a new $161 million senior secured credit facility.

As a result of our contractual and operational relationship with BRMG and Dr. Berger, we are required to include BRMG as a consolidated entity in our consolidated financial statements.

Results of Operations

The following table sets forth, for the periods indicated, the percentage certain items in the statement of operations bears to net revenue.

	Nine months ended July 31, 2005		Nine months ended July 31, 2006	
Net revenue	100.0	%	100.0	%
Operating expenses:				
Operating expenses	75.7		74.9	
Depreciation and amortization	12.2		10.3	
Provision for bad debts	2.6		4.0	
Loss on disposal of equipment, net	0.7		0.1	
Total operating expense	91.2		89.3	
Income from operations	8.8		10.7	
Other expense (income):				
Interest expense	12.1		12.1	
Loss (gain) on debt extinguishment, net	(0.5	)	1.8	
Other income	(0.1	)		
Other expense			0.7	
Total other expense	11.5		14.6	
Loss before equity in income of investee	(2.7	)	(3.9	)
Equity in income of investee				
Net loss	(2.7	)	(3.9	)

Nine Months Ended July 31, 2005 Compared to the Nine Months Ended July 31, 2006

During the last nine months, we continued our efforts to enhance our operations and expand our network, while improving our financial position and cash flows. Our results for the nine months ended July 31, 2006 were affected by the opening and integration of new facilities, the restructuring of our existing line of credit, notes payable and capital lease obligations, increases in capitation reimbursement and our continuing focus on controlling operating expenses. As a result of these factors and the other matters discussed below, we experienced an increase in income from operations of $3.3 million, but due to a increases in interest expense, a legal settlement and costs related to our debt restructuring, we also increased our net loss by $1.7 million for the nine months ended July 31, 2006 when compared to the same period last year.

We had a working capital deficit of $557,000 at July 31, 2006 compared to a $143.4 million deficit at October 31, 2005, and had losses from operations of $4.6 million and $2.8 million for the nine months ended July 31, 2006 and 2005, respectively. We also had a stockholders deficit of $74.6 million at July 31, 2006 compared to a $70.6 million deficit at October 31, 2005.

The working capital deficit as of October 31, 2005 included the reclassification of approximately $109 million in notes and capital lease obligations as current liabilities expected to be refinanced. We were subject to financial covenants under our debt agreements and believed we may have been unable to continue to be in compliance with our existing financial covenants during fiscal 2006. As such, the associated debt was reclassified as a current liability.

Effective March 9, 2006, we completed the issuance of a $161 million senior secured credit facility that we used to refinance substantially all of our existing indebtedness (except for $16.1 million of outstanding subordinated debentures and approximately $5 million of capital lease obligations). We incurred fees and expenses for the transaction of approximately $5.6 million. Debt issue costs are being amortized on a straight-line basis over 65 months and are included in other assets. In addition, we recorded a net loss on extinguishments of debt of $2.1 million, which includes $1.2 million in pre-payment penalty fees that are unpaid as of July 31, 2006 and classified as accrued expenses under

current liabilities. The facility provides for a $15 million five-year revolving credit facility, an $86 million term loan due in five years and a $60 million second lien term loan due in six years. The loans are subject to acceleration on December 27, 2007, unless we have made arrangements to discharge or extend our outstanding subordinated debentures by that date. We intend to retire the subordinated debentures prior to their due date of June 30, 2008. Under the terms and conditions of the new Second Lien Term Loan, subject to achieving certain leverage ratios, we have the right to raise up to $16.1 million in additional funds as part of the Second Lien Term Loan for the purposes of redeeming the subordinated debentures. Additionally, under the current facilities, we have the ability to pursue other funding sources to refinance the subordinated debentures. The new loans are payable interest only monthly except for the $86 million term loan that requires amortization payments of 1.0% per annum, or $860,000, paid quarterly.

On July 6, 2006, Primedex entered into an agreement and plan of merger for the acquisition of Radiologix, Inc. by Primedex through the merger of a wholly-owned subsidiary of Primedex with and into Radiologix. Upon successful completion of the merger, Radiologix stockholders will receive a combination of cash and Primedex common stock in exchange for their shares of Radiologix common stock. Pursuant to the merger, Radiologix stockholders will receive aggregate consideration of 22,621,922 shares of Primedex common stock and $42,950,000 in cash. Based upon the August 17, 2006 closing price of Primedex common stock of $1.57, each Radiologix stockholder would receive $1.85 in cash for each Radiologix share, plus one share of Primedex common stock for total consideration valued at $3.42 per share. The merger agreement also provides Primedex the option to elect to reduce the share consideration by up to 3.5 million shares and to increase the cash consideration by $2 per share, provided that Primedex advises Radiologix of its election prior to the mailing of the proxy statement. Upon completion of the merger, we estimate that, subject to adjustment as described above, Radiologix s former stockholders will own approximately 34.9% of the then-outstanding shares of Primedex common stock, based on the number of shares of Radiologix and Primedex common stock outstanding on August 17, 2006. Primedex s stockholders will continue to own their existing shares. In connection with the proposals set forth in this joint proxy statement/prospectus, Primedex stock may be subject to transfer restrictions which are necessary to preserve Primedex s unrestricted use of its net operating loss carry-forwards.

Primedex has signed a commitment letter with GE Commercial Finance Healthcare Financial Services for a $405 million senior secured credit facility. The facility is expected to be used to finance the merger, to refinance existing indebtedness, to pay transaction costs and expenses relating to the merger and the credit facility and to provide financing for working capital needs post-merger. Consummation of the financing is a condition to the closing of the merger. The facility will consist of a revolving credit facility of up to $45 million, a $225 million term loan and a $135 million second lien term loan. The revolving credit facility will have a term of five years, the term loan will have a term of six years and the second lien term loan will have a term of six and one-half years. Interest is payable on all loans initially at an Index Rate plus the Applicable Index Margin, as defined. The Index Rate is initially a floating rate equal to the higher of the rate quoted from time to time by The Wall Street Journal as the base rate on corporate loans posted by at least 75% of the nation s largest 30 banks or the Federal Funds Rate plus 50 basis points. The Applicable Index Margin on each the revolving credit facility and the term loan is 2% and on the second lien term loan is 6%. Primedex may, after a certain period, request that the interest rate instead be based on LIBOR plus the Applicable LIBOR Margin, which is 3.5% for the revolving credit facility and the term loan and 7.5% for the second lien term loan. It is anticipated that the credit facility will include customary covenants for a facility of this type, including minimum fixed charge coverage ratio, maximum total leverage ratio, maximum senior leverage ratio, limitations on indebtedness, contingent obligations, liens, capital expenditures, lease obligations, mergers and acquisitions, asset sales, dividends and distributions, redemption or repurchase of equity interests, subordinated debt payments and modifications, loans and investments, transactions with affiliates, changes of control, and payment of consulting and management fees. The credit facility will contain such conditions to funding as are customary for senior secured facilities of this type.

Net Revenue

Net revenue for the nine months ended July 31, 2006 was $118.5 million compared to $105.5 million for the same period in fiscal 2005, an increase of approximately $13.0 million, or 12.3%.

In addition to new capitation contracts, we have continued to improve our yield from capitation as a result of contractual and negotiated increases in reimbursement coupled with improved collections of co-payments from the individual patients. For the nine months ended July 31, 2006 and 2005, net capitation revenue, including co-payments, was $32.1 million and $27.8 million, respectively, an increase of approximately $4.3 million. In addition, net revenue increased for the nine months ended July 31, 2006 due to increased marketing efforts, new contracts, maturing centers, pull-through or referred business from expanding capitation arrangements, expansion of existing facilities and new satellite locations.

During the nine months ended July 31, 2006, the largest net revenue increases were at the Temecula and Tarzana facilities with combined increases of approximately $5.5 million when comparing results with the same period last year. Tarzana s continued growth is due to hiring of key physicians in the region, the location of the facilities, the increased utilization of PET, increased marketing efforts and state of the art medical equipment. The Temecula facilities continued growth is due to a variety of factors including their physical locations, the return of a large capitation agreement,

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improvements in contracted reimbursement, the opening of additional satellite facilities, the ramp-up of the Murrieta site which opened in December 2004, and increases in patient volume and throughput.

The largest net revenue decrease was at the Beverly Hills facilities with a decrease of approximately $0.8 million when comparing results with the same period last year. The decrease was due to increased competition in the area.

Operating Expenses

Operating expenses for the nine months ended July 31, 2006 increased approximately $9.6 million from $96.2 million during the nine months ended July 31, 2005 to $105.8 million during the same period this year.

The following table sets forth our operating expenses for the nine months ended July 31, 2005 and 2006 (dollars in thousands):

	Nine Months Ended July 31,	
	2005	2006
Salaries and professional reading fees	$ 49,122	$ 55,719
Building and equipment rental	5,837	6,325
General administrative expenses	24,833	26,657
Total operating expenses	79,792	88,701
Depreciation and amortization	12,905	12,175
Provision for bad debt	2,789	4,739
Loss (gain) on disposal of equipment, net	698	210

- ***Salaries and professional reading fees***

Salaries and professional reading fees increased $6.6 million, or 13.4%, for the nine months ended July 31, 2006 when compared to the same period last year. The majority of the increase is due to the $13.0 million, or 12.3%, increase in net revenue that included the variable labor necessary to service the additional patient volume, the additional locations, and the compensation to physicians with contracted fees based upon a percentage of net revenue. During the third quarter of fiscal 2006, we incurred approximately $500,000 in additional salaries for several physicians and supporting operational staff that we and BRMG hired in advance of several new acquisitions scheduled to open in the fourth quarter (see Note 6). In addition, during the nine months ended July 31, 2006, we recorded stock-based compensation expense of $345,000 for the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Stock-based compensation expense included compensation expense for share-based payment awards granted prior to, but not yet vested as of October 31, 2005 based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS 123. No stock-based compensation expense was recognized in the nine months ended July 31, 2005.

- ***Building and equipment rental***

Building and equipment rental expenses increased $0.5 million for the nine months ended July 31, 2006 when compared to the same period last year. The increase is primarily due to the additional of building rental expense for the new centers in Emeryville, Westlake and additional satellite facilities coupled with annual increases in base rentals from previously existing leased facilities.

- ***General and administrative expenses***

General and administrative expenses include billing fees, medical supplies, office supplies, repairs and maintenance, insurance, business tax and license, outside services, utilities, marketing, travel and other expenses. Many of these expenses are variable in nature. These expenses increased $1.8 million during the nine months ended July 31, 2006 when compared to the same period last year. The increase is primarily due to the $13.0 million increase in net revenue and the related variable general and administrative expenses necessary to service the additional patient volume, and other expenses that are based upon a percentage of net revenue, including equipment maintenance. The equipment maintenance agreement fees increased from 3.50% of net revenue in fiscal 2005 to 3.62% of net revenue in fiscal 2006.

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- ***Depreciation and Amortization***

Depreciation and amortization decreased by $0.7 million for the nine months ended July 31, 2006 when compared to the same period last year. At July 31, 2005, net property and equipment was $71.0 million compared to $62.8 million at July 31, 2006.

- ***Provision for bad debt***

The $1.9 million increase in the provision for bad debt for the nine months ended July 31, 2006 when compared to the same period last year was primarily a result of increased revenue coupled with a change in timing of writing off older accounts receivable.

- ***Loss on disposal of equipment, net***

The $0.2 million loss on the disposal of equipment for the nine months ended July 31, 2006 was primarily due to the write-off of $143,000 in leasehold improvements at the Emeryville facility which was closed with the opening of the new facility in the third quarter of fiscal 2006. The $0.7 million loss on the disposal of equipment for the nine months ended July 31, 2005 was primarily due to the trade-in of an MRI and replacing the equipment with an enhanced machine which improved throughput and volume demands at one of our Tarzana facilities.

Interest expense

Interest expense for the nine months ended July 31, 2006 increased $1.6 million when compared to the same period last year. The increase was primarily due to the restructuring of our line of credit, notes payable and capital lease obligations in March 2006 and the financing of an additional $5.6 million in transaction fees coupled with a slightly higher weighted average interest rate during the period. During the nine months ended July 31, 2006, we incurred a mark to market interest expense adjustment of approximately $0.4 million. As part of the refinancing, we were required to swap at least 50% of the aggregate principal amount of the facilities to a floating rate within 90 days of the close of the agreement on March 9, 2006. On April 11, 2006, effective April 28, 2006, on $73.0 million (one half of our First and Second Lien Term Loans of $146.0 million), we entered into an interest rate swap fixing the LIBOR rate of interest at 5.47% for a period of three years. Previously, the interest rate on the $73.0 million was based upon a spread over LIBOR which floats with market conditions.

Loss (gain) on debt extinguishments, net

In the nine months ended July 31, 2005, we recognized gains from extinguishments of debt for $0.5 million for the write-off of certain notes payable past statute for $475,000 and the settlement of other notes payable at a discount of $40,000. During the nine months ended July 31, 2006, due to the March 2006 debt restructuring, we recognized a net loss on extinguishment of debt of $2.1 million that is comprised of a gain of $2.1 million for a discount on notes payable, offset by $2.1 million in pre-payment penalties and $2.1 million for the write-off of capitalized debt issue costs.

Other Income

In the nine months ended July 31, 2005, we earned other income of $0.2 million. During the nine months ended July 31, 2005, we recognized gains from write-off of liabilities previously expensed in fiscal 2004 for approximately $62,000, deferred rental income of $67,000, and record copy income of $44,000. We had no other income during the nine months ended July 31, 2006.

Other Expense

In the nine months ended July 31, 2005 and 2006, we incurred other expense of $25,000 and $0.8 million, respectively. During the nine months ended July 31, 2005, we recognized losses on the write-off of other assets of $25,000. During the nine months ended July 31, 2006, we recorded expenses of $788,000 that include the $500,000 settlement with Broadstream and related legal fees.

Equity in Income of Investee

In the nine months ended July 31, 2006, we earned income for our 47.5% investment in a PET center of approximately $61,000. The investment of $237,000 was made in February 2006.

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Results of Operations

The following table sets forth, for the periods indicated, the percentage certain items in the statement of operations bears to net revenue.

	Three months ended July 31,			
	2005		**2006**	
Net revenue	100.0	%	100.0	%
Operating expenses:				
Operating expenses	74.1		74.6	
Depreciation and amortization	11.7		10.1	
Provision for bad debts	2.6		5.0	
Loss on disposal of equipment, net			0.5	
Total operating expense	88.4		90.2	
Income from operations	11.6		9.8	
Other expense (income):				
Interest expense	11.8		13.4	
Other income	(0.1	)		
Total other expense	11.7		13.4	
Loss before equity in income of investee	(0.1	)	(3.6	)