

Assure Holdings Corp. (IONM) CEO John Farlinger on Q2 2022 Results - Earnings Call Transcript

Assure Holdings Corp. (NASDAQ:[IONM](#)) Q2 2022 Earnings Conference Call August 15, 2022 4:30 PM ET

Company Participants

Scott Kozak - Director of Investor Relations

John Farlinger - Executive Chairman & Chief Executive Officer

John Price - Chief Financial Officer

Conference Call Participants

Jim Sidoti - Sidoti and Company

Scott Henry - ROTH Capital

Operator

Good afternoon, and welcome to the Assure Holdings' Second Quarter 2022 Earnings Call. All participants will be in a listen-only mode [Operator Instructions]. Please note this event is being recorded.

I would now like to turn the conference over to Scott Kozak. Please go ahead.

Scott Kozak - Director of Investor Relations

Hello, everyone. Thank you for participating in today's conference call to discuss Assure's Holdings' financial results for the second quarter 2022. On the call today are Executive Chairman and CEO, John Farlinger; and CFO, John Price. After market closed this afternoon, the company issued a press release announcing its results for the second quarter 2022. The release and investor presentation are available on the Investors section of our website.

Before we begin the prepared remarks, I would like to remind you that some of the statements made will be forward-looking and are made under the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those projected or implied due to a variety of factors. We refer you to Assure's recent filings with the SEC, including our quarterly report on Form 10-Q for the fourth quarter and full year for a

more detailed discussion of the risks that could impact the company's future operating results and financial condition.

Also on today's call, management will reference certain non-GAAP financial measures, which we believe provide useful information for investors. For a reconciliation of these non-GAAP measures, please consult the most recently filed 8-K associated with the filing of the earnings release for the three months ended June 30, 2022, which is available on the SEC website.

Finally, I would like to remind everyone who dialed into the call by telephone, you may want to join our webcast or download our second quarter 2022 earnings presentation on Assure's Investor Relations site found at ir.assureneuromonitoring.com in order to see the slides referenced today. This call will be recorded and made available for replay via link on the company's website.

Now I would like to turn the call over to the Executive Chairman and CEO of Assure Holdings, John Farlinger. John?

John Farlinger - Executive Chairman & Chief Executive Officer

Thank you, Scott. Hello, everyone and thanks for joining us today. On Slide 3, you see the agenda of key topics we'll cover on today's earnings call. We're going to start with a discussion of recent corporate developments, talk about revenue cycle management, talk about the actions we've taken and continue to take to improve profitability and then discuss cash receipts. John Price will walk you through a Q2 financial summary as well as discussing accounts receivable trends and I'll conclude with setting expectations for the second half of 2022.

I'll begin with a review of recent corporate developments. Today, we will show why Assure's second quarter and first half were strong operationally, challenging on an accounting basis and ultimately have laid important groundwork for what we believe will be a significantly stronger, more financially stable second half of 2022 and beyond.

Assure outperformed in managed case volume and cash collections during the quarter, underscoring the growth and underlying strength of our business. We also took steps to become leaner and more profitable. Assure began a strategic cost reduction effort that we expect will yield over \$4.5 million of annualized savings. As a result, we expect to become cash flow positive on an adjusted operating basis as our business becomes leaner and profitable in the second half of 2022. And despite this cost cutting, Assure continues to expect to meet its guidance of performing 25,000-plus managed cases in full year 2022, an increase of more than 40% from 2021.

Finally, we formalized a new accounts receivable accrual and reserve strategy. This led to a higher-than-anticipated reserve because we chose to take a conservative approach when reserving accounts receivable in the second quarter. The issue here is not lower reimbursement, negatively impacting our accrual rates. Our accrual rates in high-volume

markets have remained stable. Rather, we chose to be conservative on reserving accounts receivable, given our visibility on the challenges associated with collecting certain receivables before they are automatically reserved at 24 months in the third and fourth quarters of this year.

The benefit of taking these reserves now and front-loading the process is: number one, it provides clear visibility into future accounts receivable write-down expenses. And two, our anticipated second half exposure is forecasted to be less than \$4 million. The health care collections disruption experienced in 2020 associated with the onset of COVID-19 was highly unusual and widespread. Legislation has extended the timeline to pursue these receivables, and we expect to recover a portion of these accounts receivable reserves in the upcoming quarters.

Next on Slide 5 I'll provide more detail on the current status of Assure's revenue cycle management function and our overall billing and collections efforts. As we noted on our first quarter earnings call, Assure's second quarter results were negatively impacted by an accounts receivable reserve accounting charge. Assure made the proactive decision to approach this matter conservatively with regards to accounts receivable reserve accounting charge in the second quarter, including all volume reasonably considered at risk. This is associated with the long-standing company policy to reserve receivables that have aged 24 months, plus an estimate of what we do not expect to collect through the second half of 2022. We forecast that our potential exposure from major receivables in the second half will be less than \$4 million, and potentially meaningfully lower, as we continue to pursue payment on these claims during the third and fourth quarters.

The context for this is that the company brought its revenue cycle management function in-house after taking over from a third-party provider in early 2020 amid the disarray of the onslaught of COVID-19. A segment of the claims in this period had data issues and others were generally not handled quickly or effectively enough. In addition, there was a slowdown in reimbursement seen across not only the entire interoperative neuromonitoring industry, but the health care industry in general.

We have learned from this experience installed new leadership in this group and to up a tactical team to specifically work these reserve claims. Our revenue cycle management team is working hard to resurrect these files from decline status to activated. And ultimately, we expect to recover a meaningful share of cash receipts from these fully reserved receivables with early returns anticipated in the second half of 2022 and carrying over into 2023.

Recovery of these reserve and written down receivables will be reported as net new revenue and additional margin in the period collected with almost no corresponding costs because the amounts have already been fully reserved. We expect that this problem will be significantly reduced in the near-term and in 2023.

I'd also note that Assure's collections have been strengthened by our greater than anticipated success engaging in independent dispute resolution processes on contested claims. Not only has this benefited cash collections going forward, it will also strengthen our accrual rates.

Looking out into the third and fourth quarters of 2022 and into 2023, the company will have the benefit of our managed case growth, ongoing success on the dispute resolution front and removing the cloud of material accounts receivable write-downs.

On slide 6, I provide additional detail on actions we've taken to drive down costs and improve long-term profitability. Given the current economic and capital markets environment, the company has substantially reduced our structural costs, including roughly 20% of our workforce, enabling Assure to realize over \$4.5 million of annualized savings.

In addition, a key focus for Assure in the second half of 2022 will be on reducing the company's average cost of delivery in providing our services both on the technologist and the remote neurology parts of our business.

As a result, we expect to become adjusted operationally cash flow positive as our business becomes leaner and we will be profitable in the second half of this year. This reflects our focus on becoming self-sustaining from a cash flow perspective, as well as the investments we are making to continue collecting cash in record amounts.

It also highlights our decision to prune certain markets where we were not getting the desired returns. However, even with running leaner, again, we anticipate hitting our managed case volume of 25,000 in 2022, a record number representing an increase of more than 40% compared with our 2021 volumes.

On slide 7, you will see Assure's dramatic increase in total cash collections over a trailing six, 12 and 24-month plus period. For accounts receivable generated from 100% owned Assure entities, the company is collecting more than 65% in the first six months after they were issued, and more than 85% in the first 12 months after they were issued. Both of these represent record rates for the company.

We are collecting what we are accruing on the front end. In fact, we think we may be able to improve those numbers beyond what we've accrued. We are driving higher participation rates, shortened cash cycles and better collections. This will ultimately result in improved network contracting. Accelerating our cash flow reduces our need for working capital and also serves to minimize reserves in the future.

To add more color to a comment I made earlier. What happened in health care billing in 2020 around the onset of COVID was really a once in a generation disruption. However, with a sophisticated data driven revenue cycle management function in-house for Assure that disruption is now behind us, and we are now collecting rapidly. Unfortunately for many of our competitors in the neuromonitoring space, many of

whom still depend on third-party billing providers that struggle will continue for some time to come.

Laws have been put into effect as a result of the COVID disruption to health care billing that will now extend the window for collecting 2020 unpaid claims, and we absolutely expect to recover some of the accounts receivable reserve during the upcoming quarters.

Next, John Price will walk us through the quarterly financials. John?

John Price - Chief Financial Officer

Thanks John and thank you everyone for joining us today. On Slide 8, I will provide color on financial results from our second quarter 2022. Assure continued to generate strong procedure growth up 36% to 5,800. As John mentioned, Assure reported gross revenue of \$9.2 million and net revenue of \$1.6 million, adjusted EBITDA loss of \$5.9 million and net loss of \$4.7 million.

The previously mentioned reserve of aged receivables was netted against current quarter revenue and negatively impacted our financial results. Further, Q2 typically experiences seasonality due to a less favorable revenue mix between government and commercial insurance, which reverses as the year progresses and case volumes increase. Our revenue accrual rate has remained stable in our key high-volume markets reinforcing our business fundamentals and revenue recognition.

Our operating expenses decreased to \$4.1 million, compared to \$4.5 million. And as referenced earlier, we expect operating expenses to be further reduced in the third and fourth quarters.

Next on Slide 9, we will look at days sales outstanding. In this table, we see that Assure's DSOs have decreased dramatically from nearly 600 days during a COVID impacted 2020 to 311 days in the second quarter of 2022. We are simply collecting cash faster. As a result, there is significantly reduced exposure to future accounts receivable reserves. While we are pleased with the reduction in DSO, there is still room for improvement. We are focused on driving this significantly lower from current levels.

Next on Slide 10. We will look at trends in accounts receivable aging by quarter. Comparing the time periods, you can see that in the second quarter Assure had 83% of its outstanding accounts receivable in the 12 months or less bucket. In comparison during the first quarter of 2022 just 68% of accounts receivable was categorized as 12 months or less. What that shows is by the end of the second quarter a much larger proportion of our accounts receivable are in what we consider a current bucket of 12 months or less. The shift of the accounts receivable towards the current bucket reduces Assure's exposure and susceptibility to future reserves. And as John mentioned earlier, we are collecting what we are accruing on the front end. We have turned the corner here and minimize the risk of this type of reserve occurring again.

Now I will pass the call back over to John Farlinger for expectations on the second half of 2022. John?

John Farlinger - Executive Chairman & Chief Executive Officer

Thanks John. On Slide 11, we are going to do something that we have not done before, which is to provide guidance. This guidance will be for the second half of 2022. This information is presented, because we want to be clear and transparent about our expectations for the remainder of the year. We expect the third quarter and fourth quarter to be much cleaner quarters compared with the first half of 2022.

Starting at the top, we see continued strength in managed case volume with an acceleration happening during the second half of the year. Our visibility into our markets is strong, given the recurring nature of our work with surgeons, as well as our exceptional surgeon retention rate.

The accounts receivable reserve accounting charge we absorbed in the first and second quarters masked the fact that Assure generated over \$18 million in gross revenues. In the second half of 2022, we expect revenue to accelerate. The drivers here include seasonality. We anticipate that the company's managed cases will follow the familiar pattern of a continued ramp-up from the second quarter to progressively busier third and fourth quarters. Similarly, our revenue mix reflects the seasonality. And with the first two quarters typically representing our highest percentage of cases with patients utilizing government insurance and the third and fourth quarters seeing the mix become progressively tilted toward more profitable commercial insurance patients. We expect both seasonality trends to continue over the balance of 2022.

On top of these seasonal tailwinds, we also have the upside potential of sizable new business wins associated with facility-wide outsourcing agreements relating to the GPO, organization agreements with group purchasing organizations including Premier and others, Assure has signed. We also are looking at multiple M&A opportunities.

As I mentioned earlier many of our peers will continue to struggle to collect money. And we see quite a few interesting opportunities in the market even today. As we look into the second half of the year, we have forecasted less than \$4 million in accounts receivable reserve accrual which of course is substantially reduced risk compared with the reserves we took in the first two quarters of 2022.

We expect the AR reserve in the second half of the year to be roughly equally distributed between the third and fourth quarters. Therefore, in the second half of 2022, we anticipate a much narrower gap between gross revenue and net revenue compared to what we saw in the first half of 2022.

On the cost side, beginning in the third quarter and accelerating in the fourth quarter Assure will see a sharp reduction in operating costs. As we benefit from the administrative cuts we have made. Further, we won't be burdened by the severance

expenses associated with actions taken earlier this year to make the business leaner. I also want to highlight that we do not anticipate expanding our corporate staff to meet the company's growth in 2022 and 2023.

Finally, we see continued strength in collections as we further accelerate collections on new claims and improved collections on aged receivables. Taken together, Assure will have significantly reduced accounts receivable reserves and a substantially lower cost structure coupled with an increase in managed case volume. This will ultimately drive higher revenue and margins, and we believe, positive adjusted EBITDA and operating cash flow during the second half of 2022.

I want to reiterate that the opportunities ahead of us with remote neurology services and group purchasing organizations, organic expansion into new and existing states, our channel program and our commitment to clinical excellence will keep us busy over the balance of 2022.

I have had a long career in business, including helping to lead four successful turnarounds. Assure navigated a much more challenging COVID impact in 2020. We will navigate the current situation and come out of this much stronger. The foundation for the future profitability of our company is firmly in place.

And with that, I'll turn the call back to our operator for Q&A.

Question-and-Answer Session

Operator

Thank you. We will now begin the question-and-answer session. [Operator Instructions] Our first question comes from Jim Sidoti with Sidoti & Company. Please go ahead.

Jim Sidoti - Sidoti and Company

Hi. Good afternoon and thanks for taking the question. You've taken reserves in the past. This one is actually a little bit less than some of the one you took in 2020. Is this getting to the end of the line at this point don't you think?

John Farlinger - Executive Chairman & Chief Executive Officer

Jim, it's John. I hope we're at the end of the line. This reserve was different than the one we took in 2020. And you may remember in '20, we were dealing with really the collapse of reimbursement numbers. We proactively wrote down our accounts receivable in response to what we saw as a continued projection to lower reimbursement.

In this case, like a lot of our competitors, we were faced with reimbursement numbers that were very challenging coming out of the COVID period in 2020. That was one challenge. The second was quite simply part of our revenue cycle management team

wasn't good. I am not going to make excuses. We went through this in the first quarter discussion. We told everyone then that this would linger into the second quarter. We can't change what's happened, but we're sure going to affect what's going to happen going forward.

And as you look at forecasting the reserves going forward and you look at John Price's information, you see our exposure to accounts receivable and bad debt being significantly reduced because of the fact that we're collecting so much more in the front end in the first six months, nine months 12 months. So, you're not going to have 600 days of AR, you're going to have 300 days hopefully going to 200 days over the next 12 months, and we're not going to be as susceptible to this type of exposure.

The other thing I'll say is like we did in 2020, we collected millions of dollars after the fact after those amounts were written off and we expect to do the same thing in the second half of this year. And we expect that it will have a meaningful impact, as its net new revenue and new margin for us going forward.

Last thing I'll say is, we made some changes on our revenue cycle management team. I want to emphasize, this doesn't take away from the success we've had on the front end and how good our team is at getting through invoicing, dealing with new billing, getting a QR system, negotiating, settling arbitrating cases. We're pretty good at it. And as we look at other M&A targets, we don't see anybody being better. But we dropped the ball going back to 2020. And I think we're at the end of the road here in terms of the reserves, once we get through the second quarter.

Jim Sidoti - Sidoti and Company

So just to be clear, if you haven't taken the reserve, revenue for the quarter would have been over \$9 million with gross margins over 56%. Is that the kind of gross margin we should anticipate over the next four or five quarters?

John Farlinger - Executive Chairman & Chief Executive Officer

I think it would probably be unrealistic to think you won't have any reserves. Everybody in out-of-network billing is going to have some reserves. But I think a margin exceeding 50% would be expected.

And I would hope that we're back to the reserve numbers that we saw in the second half of last year, where we're writing off \$1 million to \$2 million per quarter as kind of an expectation. And then with the assumption that we're following up immediately to try to recover the AR that falls off after 24 months.

The good news, as John Price went through in his analysis, is we have not seen a degradation in what we're accruing. In fact, I think, because of the success we're having in settling and arbitrating cases, we're actually seeing those numbers holding pretty firm in our key states. So that's been fairly encouraging for us.

The other thing that I just want to articulate is we're getting away from the model of sharing revenue with surgeon partners. We are getting into one where we're simply going after the facilities and keeping all that professional revenue.

And as you wean yourself off of the old model, that will only bolster margins and improve our margins particularly on the side of generating professional revenue, which we see as really a key component going forward, driving more and more neurology-based professional revenue.

Jim Sidoti - Sidoti and Company

And you gave some pretty specific guidance for the second half in revenue. What gives you the confidence that you'll hit that number? And does that number include recovering some of the reserves that you took in the first half of the year, or is that just from procedure growth in the second half of the year?

John Farlinger - Executive Chairman & Chief Executive Officer

Yes. The revenue numbers -- well, there's three or four factors that enter in our assessment of the forecast for the second part of the year -- the first is simply rate times volume, number of procedures times our accrual rates. It's pretty predictable. Now, as we bring on surgeons and new facilities and we've got that model down to each surgeon at each facility across all of our markets. The second part is will you see any difference in the accrual rates. We don't think so. We haven't seen much of a degradation in the last 12, 18 months.

The third issue then is what the reserve is going to be. And we forecasted that we know what our worst case is now. If we collect nothing on those old accounts receivable and it's nowhere near what we've written off already - and we're collecting on those accounts receivable.

The last thing is we've significantly cut our cost structure. And by Q4, you will see an overhead structure that's roughly 60% of what it was in Q1. We have run lean. The management team is taking reductions in salaries. Middle manager are doing the same thing. And we've been able to significantly reduce our overheads below the margin number. And we think you'll see the results of that in Q4 as we have a leaner business with more volume generating a higher margin.

And I think we'll be able to improve the cash acceleration in some of our business on the front-end. We're very confident of that. And as we've talked about in the past, this is a business where we need to get to volume and higher scale. And if we're not increasing the size of our overheads on the bottom line, I think we're going to have a very strong Q4 and it's going to set us up for a very strong 2023 as we get these issues behind us.

Jim Sidoti - Sidoti and Company

And it sounds like these issues aren't just affecting Assure, but they're affecting everybody in the space. Do you think that some competitors might drop out over the next 12 to 24 months?

John Farlinger - Executive Chairman & Chief Executive Officer

Sure. We hope so. I've been on calls with some of our larger competitors over the last two to three weeks. Nearly all are facing the same challenges that we had coming out of 2020, where they're taking write-offs that they weren't expecting. One of them, a private equity-backed competitor, is feeling the same challenges. but also, the same optimism going into the second part of this year. You'll see the No Surprises Act kick in the ability to arbitrate claims. And really, it's even playing field for us now, where in the past we had no choice if we didn't get paid. We had to litigate or go to the insurance commission. Now we can arbitrate, and we are arbitrating and settling claims at a rate we've never done before.

And I think that's part of the ingredients here. It comes down to the investments we've made in the past such as data analytics. Being able to go and settle these claims and using that information. And I think a lot of our competitors are not going to have that information. If they're using a third-party billing company they're going to have a tough time.

Even our larger competitors, companies that are twice our size, have not made the investments in data analytics. We've just completed a complete data warehousing overhaul of our entire business where we're getting data that nobody else is. And I think our team has been embarrassed over the numbers from Q2 and we're wearing it, but we're going to rise to the occasion in Q3 and Q4. We're going to deliver some pretty strong numbers on the back of what we built here from an infrastructure standpoint.

Jim Sidoti - Sidoti and Company

That was it for me. Thank you. Thanks again for taking the question.

John Farlinger - Executive Chairman & Chief Executive Officer

Thank you, Jim.

Operator

Our next question comes from Scott Henry with ROTH Capital. Please go ahead.

Scott Henry - ROTH Capital

Thank you, and good afternoon. Just a couple of questions. It seems like things are going pretty good right now despite the accounting noise in the first half of 2022. I mean, as far as analyzing the business, do you think the best signal is kind of -- is the

cases per quarter and the fact that that 25,000 cases for 2022, do you think that's kind of the best number in kind of a noisy time period to focus on?

John Farlinger - Executive Chairman & Chief Executive Officer

A couple of thoughts. We're pretty confident the 25,000 number is good for the second half of the year. And obviously that's driving volume.

The second part of that question is what are you getting per procedure, what is the recovery or the accrual and are you getting those accruals? And frankly our accrual rates are standing up. Our accrual rates are stronger than most of our competitors. We're looking at much stronger.

Then if you can get a yield on rate times volume and get a higher recovery per procedure, I think you're set up to be able to continue to grow your business effectively, but also integrate other businesses who are getting that same yield. And to Jim's point, I think some of our competitors are going to be challenged. They have not made the evergreen investments in their business.

And we spent a lot. It hasn't played out yet in earnings numbers, but we spend a lot of money and time and energy building this business to be able to scale to 50,000, 70,000, 80,000 procedures.

And I think in the second half of the year, you'll see a much scaled-down version of Assure and you will start to see earnings numbers that are meaningful in Q4. We'll pull out the severance numbers in Q2 to a degree in Q3. But by Q4, you'll see a scaled-out business where we're going to hit the numbers that we telegraphed would hit earlier in the year.

Scott Henry - ROTH Capital

Okay, great. And speaking of that revenue per case number, if I look at the gross revenues for the first couple of quarters of 2022 and I exclude the other revenues to get more of a reflective number. I generate numbers I think for the first quarter depending on how you calculate them of about \$1,600; in the second quarter about \$1,500. How do you think about those rates going forward? Do you -- would you expect them to contract a little bit, or do you think those are good numbers?

John Farlinger - Executive Chairman & Chief Executive Officer

No, I think you're going to see them improve. I kind of alluded to it in the discussion earlier. This business was really set up to generate revenue on the back of billing for technologists. And two years ago, really all of our revenue was generated in the back of tech billings. Only 10% or 15% of the revenue was for neurologist services.

In Q1 we did about 65% of our revenue from neurologist services. We're going to migrate most of that revenue onto our own platform and away from a rev share. As we do that, it's only strengthening our margins. And frankly, I think that's where we want to go in the second part of the year and into next year and move that number from 65% to a much higher number. Driving your average revenue per procedure up and driving your margin up. What goes with that is we're also reducing our cost of delivery and bringing our technologist cost down and driving our cost of really delivering the neurology services down as we go to scale.

The last part is as you look at the second half of the year, Scott, and you know this we -- we benefit from the seasonality of our business. In the first six months, the majority of our business is Medicare-driven and Medicaid and government funding. In the second part of the year, as deductibles kick-in, those margin numbers improved. And so you've got this continued scaling in Q3 ultimately going much higher in Q4 with higher margins.

And so we're feeling pretty good about the margin numbers and the ability to scale our business and the 25,000 procedures looks like -- well you saw 5,800 in Q2 which would suggest you're on target. If you even extrapolate that over Q3 and Q4 you're pretty close to that number. Does that help you?

Scott Henry - ROTH Capital

It does. And the final question, which I think you hit on a little bit here, but if you look at the mix between technical and professional in 2Q -- the technical drop down. I don't know if that has to do with the adjustments you're making. But long-term should we think that should get back to kind of a 75-25, 80-20 mix?

John Price - Chief Financial Officer

Yes, Scott the technical portion of the revenue you see in the Q is really related to the write-downs. And so this goes back to 2020, and at that point in time, the majority of our services were primarily tech related. And so, the reserve that we processed would have primarily impacted the technical portion of the revenue.

John Farlinger - Executive Chairman & Chief Executive Officer

Right. So that's affecting the Q2 number, but to your point you will see a larger and larger component of the revenue going forward being driven by the professional side of the business.

Scott Henry - ROTH Capital

Okay. Great. That's it for me. Thank you for taking my question.

John Farlinger - Executive Chairman & Chief Executive Officer

With no more questions appearing here, I want to thank you for attending the conference call today. On behalf of the Assure team, I'd like to thank everyone for listening to today's call.

Before concluding, I'd like to add a few last comments. And to summarize, Assure's greatest opportunities going forward include: number one, expanding our remote neurology services; two, taking full advantage of our position as a contracted provider of interoperative monitoring services, for some of the largest GPOs in the United States; three, organic growth that extends our reach within existing states, but also helps us expand into new states; four, utilizing data, analytics and automation to strengthen revenue cycle management and to facilitate the signing of new in-network agreements. Lastly, our results are going to be much better in the second half of 2022.

With that, I'm going to conclude. We thank all of you for your participation today and we look forward to speaking to you again on our third quarter earnings call. Thank you very much.