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LABORATORY INDUSTRY REPORT®

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HIGHLIGHTS

WASHINGTON G-2 REPORTS

Lab Networks Turn The Tables On Quest And LabCorp

Throughout most of the 1990s, the nation's largest commercial labs were able to win exclusive national or regional lab services contracts with managed care companies that effectively shut out hospital labs from competing for large portions of physician office business. The response from some hospitals was to work together to create regional lab networks to compete for contracts. Some of these networks never really got off the ground, but several have won contracts and are now gaining market share at the expense of Quest and LabCorp.


Joe Miles

The most recent example is Frontline Laboratory Network (Boulder, CO), which just won an exclusive contract to provide laboratory services to roughly 85,000 HMO and PPO members of PacifiCare in northeast Colorado. This region had previously been served by Quest, which is still the exclusive lab provider to PacifiCare in the rest of the state. "For the first time we have turned the tables on the national labs," says Joe Miles, general manager for Frontline.

Other lab networks that are competing effectively against the national labs include Joint Venture Hospital Laboratories in Michigan, United Laboratory Network in Upstate New York, Spectrum in North Carolina, and PacLab in Seattle. For more details, see *Inside The Laboratory Industry*, pp. 5-8.

Atherotech And LipoScience In Battle For Emerging Market Of Expanded Cholesterol Tests

An estimated 200 million routine cholesterol panels are performed each year in the U.S. with the aim of detecting heart-disease risk. But there is growing recognition among medical experts that many at-risk patients are not being detected with traditional tests. In response, several niche esoteric testing labs have developed expanded tests that can identify up to 95% of people at risk for heart disease—double the detection rate of routine cholesterol tests. At the forefront are Atherotech (Birmingham, AL) and LipoScience (Raleigh, NC) which have each developed proprietary tests and are now engaged in a battle to win distribution contracts with the nation's biggest labs. ➟ *p. 2*

Traditional cholesterol panels don't directly measure LDL, or bad cholesterol. Instead they use a formula that can be unreliable, especially if a patient's triglyceride count is high. Expanded tests not only provide a direct measurement of LDL, but they also look at size, type, and sometimes the number of LDL particles

Atherotech And LipoScience, *from page 1*

About a year ago it seemed like LipoScience and its NMR LipoProfile were on the fast track to becoming the runaway leader in expanded cholesterol testing. At mid-2002, the company was generating some $28 million per year from its NMR LipoProfile and related cholesterol tests (*i.e.*, homocysteine, high-sensitivity CRP, etc.), more than double the amount from a year earlier. Based on this growth, the company filed for an initial public offering in early 2002 with the goal of raising as much as $100 million from investors so that it could expand its marketing efforts.

But just prior to its planned IPO, LipoScience announced that its biggest customer, Quest Diagnostics, had switched to a competing lipid test offered by a small private lab named Atherotech. Test referrals from Quest had represented 27%, or $7.5 million, of LipoScience's annual revenue, and the loss forced it to cancel the IPO.

The loss of business also forced LipoScience to cut its staff from 180 employees to 155 earlier this year. And in March, the company hired Rick Brajer as its new president and chief executive. Brajer was formerly president of Becton Dickinson's clinical laboratory division. He replaced F. Ronald Stanton, who stepped down as CEO in November 2002.

Meanwhile, Roseanne Varner, chief executive of Atherotech, tells *LIR* that her company won the Quest contract by lowering the price of its expanded cholesterol test, the VAP Test. The VAP Test is performed only at Atherotech's CLIA-certified lab in Birmingham. Quest and other labs market the VAP Test and forward samples to the Atherotech laboratory. Atherotech performs the testing and bills the referring laboratory.

Varner would not disclose Atherotech's pricing to laboratories, but she did note that Atherotech is working hard to speed the adoption rate of the VAP Test through lower pricing. In terms of reimbursement from Medicare, *LIR* notes that the traditional cholesterol panel is reimbursed at $18.72 versus $34.68 for the VAP Test and LipoScience's NMR LipoProfile.

Varner observes that of the 200 million cholesterol panels performed each year in the U.S., only about 1% are performed using the advanced screens performed by Atherotech and LipoScience. "The time for shifting the market to the advanced screens is now, and we are working to reduce the costs so that can happen," she adds.

Most recently, Atherotech announced a new contract with LabCorp under which LabCorp will market the VAP Test. Varner says the agreement includes a provision for the transfer of patented testing technology to LabCorp that may allow LabCorp to become the first laboratory licensed to perform the VAP Test at its own facilities. As a result of the new contracts with Quest and LabCorp, Varner expects Atherotech's revenue to double this year to $32 million.

In response, LipoScience's Brajer tells *LIR* that the company's NMR LipoProfile deserves a higher price given that it is the only test on the market that provides both number and size of lipoprotein particles. Lipoproteins are the vehicle which

Cholesterol Test Options

Lab Company	*Test Name*	*CPT Code*	*National Limit*
Atherotech	VAP Test	83716	$34.68
LipoScience	NMR LipoProfile	83716	$34.68
Nearly all labs	traditional lipid panel	80061	$18.72

Source: *LIR*

cholesterol travels in the blood. Brajer says that clinical studies have proved that the number of lipoproteins is a significantly better predictor of cardiovascular disease than any other lipid measurement. He says LipoScience is focusing its marketing efforts on getting this message across to third-party payers and medical directors.

The Outlook For The Lab Industry, According To Dr. Soloway

On July 1, Henry Soloway, M.D., age 67, retired from his position as director of laboratories for Quest Diagnostics in Las Vegas. The move marked the end of a 33-year career in the industry that began in 1970 at Associated Pathologists Laboratories where he helped build a $100+ million laboratory that was merged with American Medical Laboratories (AML) in 1999, and then acquired by Quest in 2002. Shortly after his retirement we interviewed Dr. Soloway to get his perspective on several key issues facing the industry. Here's what he had to say:

What's your outlook for hospital outreach programs? Are they legitimate contenders against the national labs?
Outreach programs have a definite place in the lab industry. They are well suited to cater to their local communities with good service and turnaround times. Many physician offices are located right on hospital campuses and the convenience factor combined with the high comfort level physicians get from dealing with people they know make it difficult for the major commercial labs to compete with them for routine testing business.

However, the major commercial labs have the definite advantage when it comes to genetic testing. In any given geographic market, it's unlikely that the referral patterns will be large enough for a hospital lab or small independent lab to bring various genetic tests in-house. In most cases, the required investments in lab space, equipment, reagents, and specialized personnel are too great to be covered by the limited test volume available in their geographic market.

In addition to the national referral patterns that the major commercial labs attract, they also enjoy significantly lower costs for reagents and supplies. In many cases the reagent costs for hospital labs and small independents are by themselves more than the prices they pay to have certain genetic tests done by a commercial lab.

The other advantage the larger commercial labs have is in computer systems. They have the money to staff in-house programming departments that can build and maintain customized telephone systems, billing processes, and Internet-connectivity solutions. Hospital labs and smaller independents are less able to invest in these systems or must purchase off-the-shelf systems that may not be well suited to their needs.

"The lab business is a slow-growing mature industry. In order to grow, you've got to take away a customer from somebody else" says Soloway

What's the outlook for more joint ventures between commercial labs and hospitals?
The key is developing relationships where both sides can benefit. A commercial lab with a big position in a certain market has no incentive to share it with a hospital, and the reverse holds true for hospitals with leading positions.

How would the initiation of a 20% lab co-pay from Medicare impact the lab industry?
I can't image a worse system than having to collect two- or three-dollar co-pays for hundreds of lab tests each day. Everyone would suffer, but the major commercial labs probably have low enough cost structures to withstand the hit the best.

Most hospital outreach programs are working with thinner profit margins. They don't mind making only a little bit of money on outreach, but a co-pay could push them into losses. The costs associated with a co-pay will hit outreach programs and smaller independent labs the hardest. In fact, the lab co-pay and other potential reimbursement pressures will probably be the biggest limiting factors in how well outreach programs do in the future.

You have a lot of experience with direct-access testing to consumers. What's the key to success in this fledgling market?
You must give consumers what they want, and consumers want immediate and confidential answers to urgent questions. The demand is in the area of testing for infectious diseases like HIV and hepatitis C. There's also some demand for pregnancy testing where the home testing market has already proven itself. Consumers have a burning desire to get answers from these types of tests.

On the other hand, there is just not enough urgency for people to go out and get tested for things like a general men's health screen or a cholesterol test. So I think the test menu plays a big role in whether or not a direct-access testing program can be successful.

What's your take on the lab employee shortage?
Personnel shortages are a major issue. The average age for medical technologists throughout the country is nearing 50. Lab automation and workstation consolidation are helping to put off the day of reckoning, but at some point in the future the shortage will pose significant problems for laboratories.

You sit on the scientific advisory board of Correlogic Systems (Bethesda, MD). Tell us about Correlogic's new protein-pattern testing technology?
It's the most exciting new technology I've seen in the lab industry in decades. [The Correlogic system analyzes protein patterns rather than specific biomarkers, and studies have shown it to be 100% accurate in detecting ovarian cancer.]

Quest and LabCorp are each licensed to sell the ovarian cancer test, and commercialization should begin sometime this fall. But it will not be an inexpensive test. The equipment needed to get the test up and running in a lab costs as much as $1 million.

The jury is still out on how the adoption of the test will go. There is fierce competition for dollars from payers for new technologies. The test should sell itself, but we'll see. [Note: For complete details on Correlogic and its new ovarian cancer test see the July issue of *Diagnostic Testing & Technology Report*. For a free sample copy, send your mailing address to *labreporter@aol.com*.]

Five Lab Networks Gaining Marketshare; Project 20% Growth

Five hospital laboratory networks spread across the country tell *LIR* that they are on track to grow an average of roughly 20% this year to reach a combined $138 million in net collected outreach revenue (see table below). These networks were formed in the mid-1990s to compete for managed care contracts, which at that time were increasingly sole-sourced to the national commercial labs. Although lab networks have been slow to get off the ground, and some have failed, others are now hitting their stride and gaining access to managed care contracts they were once shut out of.

These managed care contracts (both capitated and discounted fee-for-service) generally reimburse labs at rates equivalent to 60% to 90% of the Medicare Part B fee schedule, or approximately $7 to $10 per billable test. There is some debate as to whether or not hospital labs can earn a profit on these low levels of reimbursement. But there is no debate over the fact that lab networks have offered hospitals the chance to compete on a more level playing field with Quest and LabCorp.

Meanwhile, Quest and LabCorp are being put under increasing pressure from Wall Street analysts and investors to prove they can grow their test volumes (aside from acquisitions). As a result, each company has stepped up its competitive efforts with strategies that include: 1) placing phlebotomists at physician offices; 2) opening more patient service centers to improve service; and 3) offering Internet-based order-entry and results-reporting systems.

In particular, lab network general managers tell *LIR* that the practice of placing phlebotomists is being taken to the extreme. One general manager says that the commercial labs are placing phlebotomists at physician accounts that order as little as only five tests per day. Another general manager adds, "We're being forced to match these practices, and it's eroding our profitability. This business practice has gotten to the point where it simply doesn't make sense."

Hospital Laboratory Networks

Lab Network	*Region*	*Hospitals*	*Projected Outreach Revenue for 2003*
Frontline Laboratory Network	Northeast Colorado	9	$4M
Joint Venture Hospital Laboratories	Michigan	100	$29M
PacLab	Seattle	10	$40M
Spectrum Laboratory Network	North Carolina	6	$59M
United Laboratory Network	Upstate New York	30	$6M
Totals		165	$138M

Source: *LIR*

Finally, some lab network general managers tell *LIR* that they are seeing an increased willingness on the part of both Quest and LabCorp to compete by cutting prices. "For a few years it looked like pricing was going back up, but now the downward spiral has begun again. It's a disappointing change in the marketplace. We'd rather walk away than meet

some of the bids the commercial labs are now quoting for business," observes a general manager.

Here's a closer look at how six geographically diverse lab networks are faring:

Over the past five years, **Frontline Laboratory Network (FLN)**, which includes nine hospitals in northeast Colorado and Mayo Medical Laboratories, has gained access to four managed care contracts formerly held exclusively by Quest and/or LabCorp. Joe Miles, general manager of FLN, says that the network is on track to take in about $4.4 million of net collected outreach revenue this year—a substantial increase from the $2.5 million collected in 2002.

Miles says that FLN competes with both Quest and LabCorp. Both commercial labs operate major testing facilities in Denver. He says that FLN won the PacifiCare contract for the Boulder/Ft. Collins/Greeley region even though it did not offer the lowest bid, because its network represents local hospitals and all testing is performed locally. In contrast, the Colorado operations of Quest and LabCorp are located 40 to 60 miles away from the region covered by FLN.

"There are pressures on insurance companies to offer choice so they can hold onto their members," notes Miles. He says that as part of its bidding effort, FLN commissioned a survey completed by 850 consumers in Colorado. The results showed that more than 96% preferred to have their lab tests done locally.

FLN's first contract win came in 1998, when it agreed to participate with United Healthcare as a preferred provider for 85,000 members in northeast Colorado. FLN's second contract came in March 2002, when it gained access to approximately 120,000 HMO and PPO members of Anthem under a fee-for service contract that was previously served only by Quest and LabCorp. And, in October 2002, FLN won a subcontract with Quest to provide lab services on a fee-for-service basis to Sloans Lake Managed Care (95,000 members).

Miles estimates that these three contracts, combined with the recent PacifiCare win, represent over 50% of the commercial outreach market in northeast Colorado. He cites four keys to winning managed care contracts: 1) broad geographic coverage in significant markets; 2) support and cooperation from hospital administrators and managed care contracting departments at member hospitals; 3) a proven billing and collections system designed for lab outreach; and 4) a well-developed customer service program.

In terms of new competitive pressures, Miles notes that he has seen an increased willingness on the part of the major commercial labs to place phlebotomists in physician offices as small as three or four physicians. He says that FLN is now evaluating whether its hospital members should do the same. FLN is also aiming to introduce an Internet-based order-entry and results-reporting system by year's end, he adds.

PacLab Network Laboratories (Seattle, WA) was formed in 1996 by Pathology Associates Medical Laboratories (PAML—Spokane, WA) and eight hospitals in the Puget Sound area of Washington. Stewart Adelman, general manager of PacLabs, estimates that the network has tripled its share of the physician office market over the past seven years to approximately 30%. This year he expects PacLabs to grow its net collected revenue by approximately 10% to $40 million.

PacLab competes in Seattle with Quest and LabCorp and he estimates that they each

also have about a 30% marketshare. Quest entered the Seattle area through its acquisition of SmithKline Beecham Clinical Laboratories in 1999. And LabCorp had a minimal presence until its acquisition of Dynacare earlier this year. Adelman says that all of the consolidation activity has allowed PacLab to add experienced salespeople from the commercial labs.

He says the Puget Sound area is largely free of exclusive capitated lab contracts. As a result, the competition for physician office clients is largely based on service issues such as turnaround time and the ease of billing practices. "The number one reason why a client will leave a certain laboratory is problems with billing," he notes.

Adelman says that he has not seen too much pricing pressure in the Puget Sound market, but he has seen increased efforts by commercial labs to place phlebotomists at even the smallest physician groups.

Spectrum Laboratory Network (Greensboro, NC) is on track to grow its outreach business by some 30% this year to reach $59 million, according to chief executive Nate Headley. He says that Spectrum has added a total of 210 new accounts so far this year through mid-July. Most of Spectrum's gains have come at the expense of LabCorp, which has the dominant marketshare position in North Carolina.

Headley says that LabCorp has responded to Spectrum with a willingness to place phlebotomists in small accounts and with "sharply discounted pricing." Nonetheless, Headley claims that lost business at Spectrum continues to be very small.

Headley believes that inconsistent service levels at LabCorp are the main reason physicians are switching to Spectrum, which employs 17 salespeople, including three regional sales managers.

New initiatives at Spectrum include an aggressive program to introduce an Internet-based order entry and results reporting system made by Atlas Development Corp. (Woodland Hills, CA). Headley says Spectrum is aiming to receive more than 50% of its accessions through the Atlas system by September 1.

Spectrum is a consolidated lab venture owned by Moses Cone Health System (Greensboro), High Point Regional Health System (High Point), and Novant Health System (Charlotte). It manages six inpatient labs, plus a freestanding core lab in Greensboro.

United Laboratory Network (ULN—Albany, NY) won its first two managed care contracts last year. Both are capitated contracts that pay ULN at a rate equivalent to $10 to $11 per billable test, according to network president Eric Bettinger.

One contract covers roughly 145,000 members of MVP Health Plan (Schenectady, NY); the other covers about 25,000 HMO members in Upstate New York for GHI (New York City). Combined, the two contracts represent roughly $6 million of annual lab revenue.

ULN network includes 30 hospitals that cover the Hudson Valley region of New York State. Among its owner-members are Centrex Laboratories (New Hartford), Columbia Memorial Hospital (Hudson), Ellis Hospital (Schenectady), Nathan Littauer Hospital (Gloversville), St. Clare's Hospital (Schenectady), St. Mary's Hospital (Amsterdam) and St. Peter's Health Care Services (Albany).

Other members of ULN, though they don't have ownership stakes, include Quest and MDS Hudson Valley Labs (Poughkeepsie). LabCorp is not a member of ULN.

ULN is currently in the process of bidding on two new capitated contracts: Health Now (125,000 members) and Capital District Physicians Health Plan (300,000 members). Bettinger says that LabCorp has made extremely aggressive price bids for both. "It's ludicrous. Pricing is going back to the way it was 10 years ago," he observes.

Over the past three years **Joint Venture Hospital Laboratories** (JVHL—Detroit, MI) has taken a major bite out of Quest's market leading share in Michigan.

Jack Shaw, executive director of JVHL, says the network currently has more than 14 managed care contracts covering lab services for a total of 1.6 million lives, including about 1.1 million on a capitated basis at rates that average roughly $2 to $2.25 per member per month. JVHL's larger contracts include Blue Care Network (550,000 members), Health Alliance Plan in southeastern Michigan (125,000 members), and OmniCare Health Plan (100,000 members).

This year, JVHL will collect a projected $29.4 million of net revenue, up 5% year-over-year, for its 100-plus hospital members. So far, JVHL has never lost a contract. But Shaw says Quest, which operates a major lab facility in Detroit, has been trying to win back business by offering managed care companies the opportunity to switch back to Quest at a substantial discount to JVHL's rates.

Shaw says that JVHL has been able to maintain its contracts because it offers a broader network than Quest and a higher level of service. JVHL is also able to provide managed care companies with more complete laboratory test data for HEDIS reporting, according to Shaw.

So far, JVHL has never lost a contract. "It's harder to lose a contract if you're doing a good job, and physicians don't like being dragged around by the nose [by HMOs that change their lab contracts]," adds Shaw.

Of course not every lab network in the nation is growing like gangbusters. **Regional Laboratory Alliance** (RLA—Kansas City, MO) suffered a setback when it lost a contract to provide lab services to the managed care plan HealthNet (400,000 members) last year. The decision to switch was made by Coventry Health Care, which acquired HealthNet and then consolidated all its lab contracts to LabOne (Lenexa, KS).

Meanwhile, Carla Orner, general manager for RLA, notes that RLA still has a contract with Family Health Partners (a Medicaid plan with 60,000 members), and will continue to compete for future contracts. In addition, Orner says that RLA is developing a data repository of outpatient lab tests performed by its 10 members. The information will be used to help develop lab test order guidelines for physicians, aimed at cutting down on excess utilization and improving medical decisions.

Finally, the **Preferred Laboratory Access Network** (PLAN—Carlsbad, CA) was dissolved about two years ago. This network had been formed in 1995 to go after statewide managed care contracts, but was never able to land a single contract.

After several years of unsuccessful attempts, PLAN changed gears and began creating group purchasing agreements on behalf of its 12 members, which had included ABC Labs, St. Joseph's Medical Center Labs, and Westcliff Medical Labs. But in 2000 the lab members decided the benefits weren't worth the cost or effort to keep PLAN going.

Ohio State Medical Center To Market Lab Tests At Kroger Stores

Ohio State University Medical Center (OSU—Columbus) has begun marketing a limited menu of laboratory testing services directly to consumers at the pharmacy sections at 44 Kroger supermarkets in the greater Columbus area. Based in Cincinnati, Kroger Co. is one of the nation's largest retail grocery chains with a total of 2,496 supermarkets and department stores in 32 states.

The program, dubbed "The OSU Lab Test," will allow consumers to prepay for eight different tests and panels at Kroger pharmacies and then phone one of six OSU clinics to schedule an appointment to have their blood drawn. All testing will be performed by OSU Medical Center's clinical laboratory. With a passcode, consumers will be able to view their test results at *www.osulabtest.com*. A written report will also be mailed to customers.

OSU Lab Test Menu

Test/Panel Name	Price
Women's Health Profile	$110
Men's Health Profile	$110
Nutrition Profile	$90
PSA	$45
Heart Health Panel	$75
Thyroid Profile	$45
Diabetic Profile	$45
Drug Screen	$50

Source: OSU

Test prices will range from $45 for a diabetic profile (glucose and A1c) to $110 for health profiles for men and women (cholesterol panel, hemoglobin, iron, sodium, potassium, albumin, glucose, TSH, etc.).

The OSU Lab Test program looks a lot like the direct-access testing (DAT) deal that Quest Diagnostics began with CVS drugstores in the Columbus area last year. This program was shut down after six months due to lack of interest on the part of consumers. Another DAT partnership between US Wellness Inc. (Gaithersburg, MD) and Giant Food Supermarkets was also recently terminated because of poor response (see *LIR*, July 2003, pp. 5-7).

Nonetheless, Amy Gewirtz, M.D., mediçıl director of the OSU lab, believes OSU's local name recognition and reputation will help it succeed where others have failed. She says that OSU is marketing the program in advertising circulars put out by Kroger and through "infomercials" on local radio. "We don't expect to be selling tests left and right in the begining, but we are hoping the program will become self-sustaining within the first 12 months," adds Gewirtz.

More Tips On Direct-Access Testing

The last issue of LIR focused on the challenges that Quest Diagnostics and other labs were having in their efforts to provide direct-access testing services to consumers (see *LIR*, July 2003, pp. 1, 5-7). As a follow up, we recently interviewed John Halsey, Ph.D., who founded the Personal Diagnostic Center (PDC) in Overland Park, Kansas, in February 1997.

Halsey operated PDC, which specialized in direct-access testing, for three and a half years and then sold the business to Quest Diagnostics in November 2000 so that he could pursue full-time his esoteric testing business: IBT Reference Laboratory in Lenexa, Kansas.

PDC took up about 1,200 sq. ft. at a strip mall, which was part of a major shopping area in the suburbs of Kansas City. Halsey says the most important consideration for selecting this location was convenient access to the public and visibility from the parking lot.

On its busier days, Halsey says PDC saw 15 to 20 patients. Depending on the locale and the types of promotions done, it is not unreasonable to expect $1,000 to $2,000 per day in new business from a single direct-access testing site, according to Halsey. However, he notes that even to recognize this modest level of revenue requires continued marketing and advertising expenses that the typical clinical laboratory may not have considered when creating its regular operating budget. "It is not enough to open a site and expect people to come," he adds.

Halsey says that PDC achieved its best marketing success with TV and radio advertising, while print advertising was less effective. "The key is aggressive marketing. People really don't know about this [direct-access testing]," he notes.

In addition, Halsey believes that direct-access testing centers should be staffed with nurses or medical technologists who can take test orders from customers and answer questions about tests (but not, of course, provide medical advice). "We found that customers want interaction with the laboratory," he says.

Given the expense of advertising, rent at a strip mall, salaries for a medical technologist or nurse, and finally the cost of actual laboratory testing, Halsey says that repeat customers are an absolute must if a direct-access laboratory business is to achieve profitability. He advises hospitals and independent labs entering the direct-access testing business not to expect profitability overnight. But he says that he is convinced that over the long term direct-access testing will have a significant place in the laboratory industry.

Specialty Labs Wins Consorta GPO Contract

Specialty Laboratories (Santa Monica, CA) has signed a three-year group purchasing agreement (effective July 1, 2003) for clinical reference testing with Consorta, Inc. (Rolling Meadows, IL), a group purchasing organization representing approximately 425 hospitals. Consorta also has an existing purchasing agreement with Quest Diagnostics and used to have one with American Medical Labs, which was acquired by Quest last year.

Medtox Scientific Acquires Accounts From Cox Toxicology

Medtox Scientific (St. Paul, MN) has announced the acquisition of forensic drug testing accounts from Cox Toxicology, a full-service SAMHSA-certified drug testing laboratory owned by the healthcare system CoxHealth (Springfield, MO). As of July 1, 2003, Cox Toxicology discontinued all workplace drug testing and Medtox has assumed responsibility for its accounts effective immediately. Medtox expects to generate approximately $400,000 per year from the added accounts and is paying a purchase price of less than $300,000.

Lab Stocks Up 4% In Latest Four Weeks

Stock prices for the 11 companies in the G-2 Laboratory Index rose an unweighted average of 4% in the four weeks ended July 11, 2003, with seven stocks rising in price and four falling. So far this year, lab stocks have risen 34%, while the S&P 500 is up 13%, and the Nasdaq is up 30%.

Bio-Reference Labs (Elmwood Park, NJ) was up 28% to $7.24 per share for a market capitalization of $83 million. The company now trades at 0.8 times its annualized revenue of $104 million (based on latest quarter's results).

Market Cap/Annual Revenue Valuations

Bio-Reference	0.8x
Impath	1.6x
LabCorp	1.6x
LabOne	1.2x
Medtox	0.7x
Specialty	2.0x
Quest	1.6x

Source: *LIR*

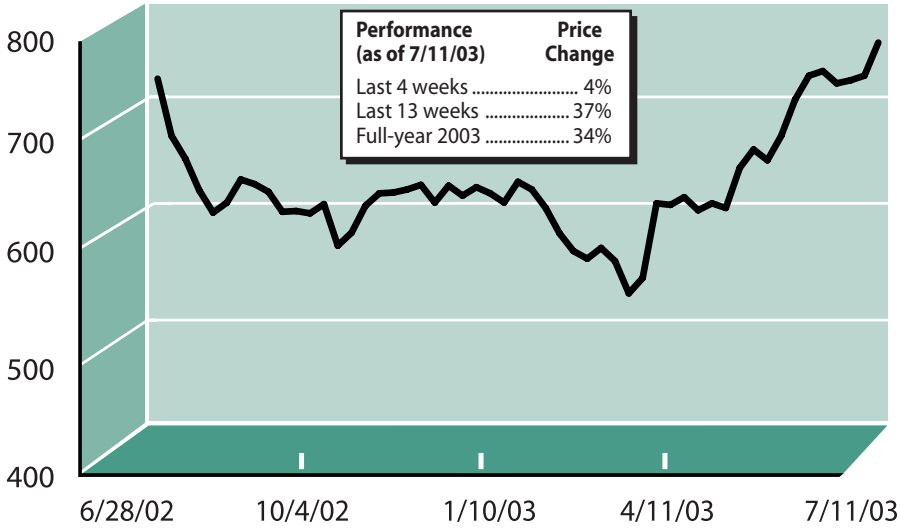
Impath (New York City) was up 24% to $17.95 per share for a market cap of $294 million—an amount equal to 1.6 times its annualized revenue of $184 million.

LabOne (Lenexa, KS) was up 17% to $23.37 per share for a market cap of $388 million—an amount equal to 1.2 times its annualized revenue of $328 million.

Meanwhile, **LabCorp** (Burlington, NC) was up 11% to $31.48 per share for a market cap of $4.6 billion—an amount equal to 1.6 times its $2.849 billion of annualized revenue. And **Quest Diagnostics** (Teterboro, NJ) was up 9% $67.02 per share for a market cap of $6.9 billion—an amount equal to 1.6 times its $4.37 billion of annualized revenue.

Among the "pure play" lab stocks, Specialty Labs currently trades at the highest multiple of its annual revenue *(see table to the left)*.

G-2 Laboratory Stock Index



Source: The G-2 Laboratory Stock Index is tabulated weekly by *Laboratory Industry Report* from the average percentage change in the price of 11 laboratory testing service stocks.

% price change, 4 weeks ended 7/11/03

UP	*Price*	*% Chg*
Bio-Reference	7.24	28
Impath	17.95	24
LabCorp	31.48	11
Lab*One*	23.37	17
Medtox	7.31	7
Specialty	10.98	4
Quest	67.02	9
DOWN		
Enzo Biochem	21.80	-21
MDS	13.27	-5
Myriad	15.76	-7
PharmChem	0.30	-12

INDUSTRY buzz

If the 20% lab co-pay becomes a reality, how much will labs actually be able to collect from Medicare recipients? For the answer to this question, we turned to Jerry Murphy, who is president of Gamma Healthcare Corp. (Poplar Bluff, MO), a privately held company that operates three labs in Missouri and a fourth in Memphis, TN.

Murphy has rare insight into this issue because each of his lab facilities also provides diagnostic imaging services. And after reaching a $100 per year deductible, Medicare recipients are today required to pay a 20% co-pay for outpatient diagnostic services. On average, Murphy says that Gamma is not able to collect on about 40% of its diagnostic imaging co-pay billings to Medicare recipients.

He thinks that if a lab co-pay were enacted, labs would face a similar rate of uncollectible billings. For example, Murphy says that his average lab claim includes 2.4 billable tests at $13.33 each for a total claim of $32. That means Gamma would be billing Medicare recipients $6.40 per claim for the average co-pay of which 40% would go uncollected. And Murphy believes the rate of uncollected debt for the lab co-pay could be even higher given that labs have no direct contact with patients.

That would be a big hit to any lab, especially when you consider that Medicare Part B lab payments often comprise one-third or more of the overall business at the typical independent lab or hospital outreach program, *LIR* observes.

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Frontline Laboratory Network
720-876-0340

Gamma Healthcare
573-785-3207

Joint Venture Hospital Labs
313-271-3692

LipoScience 877-547-6837

PacLab 452-688-9274

Spectrum Laboratory Network
336-664-6100

United Laboratory Network
518-437-0978

Regional Laboratory Alliance
913-831-2098

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