

LABORATORY

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HIGHLIGHTS

TOP OF THE NEWS

- Lab co-pay not likely 1
- LabOne to buy Alliance
- Lab Services 1-3

LAB NETWORKS/ PARTNERSHIPS

- Who's crazy enough to start their own lab? 3-4
- Stanford lab wins big IPA contract 9

INSIDE THE LAB INDUSTRY

- Lab industry winning battle against co-pay 5-8

LEGAL/REGULATORY

- Whistleblower lawsuit against Quest and LabCorp moves forward 10

FINANCIAL

- Who will buy Impath? 9
- Quest initiates dividend 11

INDUSTRY BUZZ

- Managed care consolidation could be bad news for providers 12



Lab Co-Pay Unlikely To Be In Final Medicare Reform Bill

It looks like the lab industry and its lobbyists are on the verge of a major victory. At press time, Alan Mertz, president of the American Clinical Laboratory Association (ACLA—Washington, DC), tells *LIR* that House-Senate conference committee members are leaning toward excluding a proposed 20% lab co-pay from the final Medicare reform bill they will present to Congress. “Our arguments against the co-pay are being recognized,” says Mertz.

The likely elimination of the lab co-pay in the final bill is the result of one of the most powerful lobbying campaigns ever launched by the lab industry. Most notable have been the direct lobbying efforts of ACLA and its two biggest members, Quest and LabCorp, and the grass roots movement spearheaded by the American Association for Bioanalysts (St. Louis, MO) and its independent lab members.

However, the battle is not over yet. Mertz says that conference committee members are now looking at freezing CPI updates to the Part B fee schedule for 2004 and beyond. He says the key question now is, “Will any proposed freeze be for a few years, or will it be a 10-year freeze?”

For more details, see *Inside The Laboratory Industry*, pp. 5-8. 🏠

LabOne To Buy Alliance Lab Services; Can The Culture Clash Be Avoided?

The Health Alliance (Cincinnati) has announced that it has entered into negotiations to sell its Alliance Laboratory Services (ALS) business to LabOne (Lenexa, KS). Close of the deal, which is expected by December 31, will represent one of the largest transactions ever between a hospital-owned lab system and a commercial lab. Its long-term success, which is by no means a sure thing, will be largely dependent on the ability to merge two disparate cultures (*i.e.*, the conservative, slow-moving, patient-first attitudes of a not-for-profit hospital system versus the pragmatic, bottom-line focus of a publicly traded company). Managing the transition will fall heavily on the shoulders of Wendell O’Neal, Ph.D., current vice president of ALS, and Vincent DeRisio, D.O., vice president/medical director, who are in partnership with LabOne in this potential transaction and are expected to stay on as managers after its completion. ➡ p. 2

■ **LabOne To Buy Alliance Lab Services**, *from page 1*

Under the anticipated transaction, LabOne will purchase the ALS core lab and outreach business based at the former Jewish Hospital in downtown Cincinnati. LabOne will also manage six hospital-based labs under a long-term agreement with Health Alliance, which will retain ownership of these inpatient labs.

The amount of the revenue that LabOne will earn from the transaction was not disclosed nor was the purchase price. But an informed source tells *LIR* that LabOne will add about \$36 million in annual outreach revenue from the acquisition of the core lab plus another \$9 million from a long-term agreement to provide reference testing services to the six Health Alliance hospitals. The purchase price will fall in the range of \$40 million to \$50 million, or about 1 times acquired revenue, according to our source.

Health Alliance spokeswoman Gail Myers would not comment on this speculation. However, Myers did note that ALS has a total of 800 employees and performs about 7.5 million billable tests per year. Roughly 500-600 people work at the core lab and 200-300 at the six inpatient labs.

Myers says decisions regarding how many tests might be routed to LabOne's main testing facility and headquarters in Lenexa, Kansas (a suburb of Kansas City), and the number of local jobs that might be eliminated by such a change have not been finalized. She would only say, "All parties of the negotiations are committed to treating employees fairly."

Regarding the concern that service levels and turnaround times may be hurt if large volumes of tests are shipped to LabOne's Lenexa facility, which is 500 miles from Cincinnati, Myers says the deal will include specific criteria for maintaining or improving existing quality and timeliness levels.

Why Did O'Neal and DeRisio Get Involved?

As mentioned earlier, Wendell O'Neal, Ph.D., and Vincent DeRisio, D.O., are in partnership with LabOne for the takeover of ALS and will stay on afterward to help manage the transition. Why did O'Neal and DeRisio, long-time stewards of ALS, join forces with a commercial lab? "We didn't make the decision to sell ALS. This was a process started by our CEO [Ken Hanover], who has the responsibility of looking at the economic viewpoint of the hospital system as a whole. By refusing to participate, we wouldn't have changed Ken's decision," O'Neal tells *LIR*. "We know the marketplace. We know the people. We're trying to achieve the best outcome under the circumstances," adds DeRisio.

Myers says the decision to sell ALS was based on a number of factors, including the near-term need to raise cash for significant capital needs at Health Alliance. There were also concerns about the ability of ALS to remain competitive with Quest and LabCorp over the long term, according to Myers.

What Does This Purchase Mean To LabOne?

For LabOne, the acquisition will represent its second foray into the hospital lab business. In December 2002, LabOne acquired Central Plains Laboratories

(CPL—Hays, KS) from Hays Medical Center and Park City Solutions for \$12.6 million, or about 1 times annual revenue. The pending acquisition of ALS will be almost four times bigger and will raise LabOne's revenue from healthcare testing by some 50% to an estimated \$130 million per year.

Mike Asselta, chief operating officer of LabOne, tells *LIR* that he's well aware of the spotty record that hospital/commercial lab ventures have had in the past (*see LIR, May 2003, pp. 3-4*). He says that LabOne has tried to learn from the mistakes made by others. He believes the purchase of ALS will be a success because, for one thing, ALS already operates like an independent lab. He notes that outreach programs that operate out of existing inpatient labs have proved to be difficult to manage. Asselta also believes the retention of O'Neal and DeRisio will go a long way toward smoothing relations with the ALS staff and physician customers.

Competition In Ohio Now Expected To Intensify

ALS currently services the greater Cincinnati area, and Asselta says that LabOne sees big opportunities to expand into nearby cities. He declined to identify which ones, but a glance at the map shows that Dayton (located about 40 miles north of Cincinnati) may be a target.

If this speculation is correct, then a big marketshare battle could be brewing between LabOne/ALS and CompuNet Clinical Labs (Moraine, OH), a for-profit joint venture lab owned by Quest, Miami Valley Hospital, and a local pathology group named Valley Pathologists. CompuNet, which employs 450 people and performs about 3.5 million billable tests per year, has already indicated plans to expand south toward Cincinnati (*see LIR, January 2003, p. 6*).

The Outlook For More Hospital Lab Sale/Outsourcing Deals

What's the outlook for more transactions between hospitals and commercial labs? *LIR* spoke with half a dozen industry consultants, and everyone is predicting that deal making will accelerate. "A lot of hospitals are still having financial difficulties and some are looking at selling their laboratories," observes Tom Hirsh, senior consultant at Nichols Management Group (York Harbor, ME) and former president of Path Lab Inc. (Portsmouth, NH), which was sold to LabCorp in 2001. "Deals will get done," adds Joe Plandowski, president of Lakewood Consulting Group (Lake Forest, IL). "But you've got two whole different mentalities. In the past, commercial labs have pulled out their hair trying to improve efficiency at hospital labs," he adds. ▲

Who's Crazy Enough To Start Their Own Lab?

New laboratory formations are few and far between, but some medical technologists—fed up with the bureaucracy at hospitals and sensing an opportunity to improve on the services levels provided by commercial labs—are giving it a shot. Below are profiles of two of the latest lab entrepreneurs.

THE LAB AT STEAMBOAT, LLC. (Steamboat Springs, CO) was funded with \$60,000 of cashed in retirement savings from its owner, president, and sole employee, Ken Shaffer. The shoe-string capital budget allowed Shaffer to pur-



Independent lab entrepreneurs say their biggest challenge is breaking into the exclusive managed care contracts held by Quest and LabCorp.

chase some refurbished analyzers and office equipment. The Lab at Steamboat got its CLIA certificate in May 2003 and began testing in July.

Shaffer, a medical technologist with more than 20 years' experience at two local hospitals, says he started his lab because "I was working my tail off and it was going unnoticed." He also believes that physicians and patients will recognize the benefits of having lab tests done locally rather than sending them to Denver. Currently most of the physician offices in Steamboat Springs (located in northwest Colorado) are served by Quest and LabCorp facilities in Denver, which is three hours away and often longer when the weather is bad.

Shaffer says he was also inspired by local health fairs, which indicated that a significant number of residents were willing to self pay for lab tests performed outside of normal visits to their doctor. He says his lab is currently performing tests for two to three walk in customers per day. The most requested test is a total lipid profile priced at \$25.

But Shaffer says that winning over physician office clients has proved to be more challenging. "Physicians are notorious for not changing their practice patterns," he notes. So as Shaffer waits, he says he's keeping his costs low and continuing to plug away at sales efforts to win physician business. "I do everything, including answering the phone, phlebotomy, and mopping the floor," he notes.

DIAGNOSTYX LABS LTD. (Atlanta, GA) opened its doors for business on September 2, according to Sheela Puthumana, laboratory manager and part owner. Puthumana is a medical technologist with 30 years' experience, most recently as chemistry section manager at Emory Adventist Hospital (Smyrna, GA). Diagnostyx employs another medical technologist, Jennifer Brown, and its medical director is Richard Mullins, Ph.D., who recently retired from Emory University Hospital (Atlanta, GA).

Puthumana says she started the new lab because she perceived a lack of quality and service from some of the other small independent labs in the Atlanta area. Total start-up costs were roughly \$300,000 and included the purchase of refurbished analyzers and a laboratory information system from Orchard Software Corp.

Puthumana says marketing efforts for Diagnostyx have included making cold calls to physician offices, nursing homes, and home healthcare companies from the Yellow Pages. She is also handing out business cards at local health fairs. She has already added several new nursing home and home healthcare clients, but says physician offices are more difficult to win because managed care contracts dictate where lab tests go.

Puthumana says Diagnostyx is also providing direct-to-consumer lab services and already handles one to three self-paying patients per day. To expand this line of business, Diagnostyx is planning to do some advertising in Hispanic and Asian magazines and newspapers, because these segments of the population often don't have healthcare insurance. 🏠

Lab Industry Winning Battle Against The Lab Co-Pay

It looks like the lab co-pay is off the table, but the lab industry won't know for sure until the final Medicare-reform bill is presented to Congress.

As the House-Senate conference committee works to reach a compromise on a new prescription drug benefit, it's beginning to look like the 20% lab co-pay proposal contained in the Senate's version will not be part of the reconciled bill. For this apparent victory, thanks should go out to every trade group that helped fight against it, including the industry's Clinical Laboratory Association.

It's hard to say which lobbying efforts had the greatest impact, but certainly the grass roots campaigns organized by the AAB and the massive direct-lobbying done by ACLA which represents 14 big commercial labs including Quest, LabCorp, ARUP, Specialty Labs, and Myriad Genetics, played keyed roles.

ACLA president Alan Mertz says that he as well as Quest's Ken Freeman, LabCorp's Tom Mac Mahon, and other CEOs have made numerous visits to Capitol Hill to lobby against a potential co-pay. ACLA also developed a briefing book on the lab co-pay and hired a veteran healthcare lobbyist, Denise Henry, to help fight against it. "Our direct lobbying efforts have been extremely important in combating the arguments in favor of a co-pay," according to Mertz. "A significant portion of our budget and most of my time has been spent on this issue," he adds.

One of the biggest proponents of the lab co-pay has been, of course, Sen. Charles Grassley (R-IA), who is co-chairman of the House-Senate conference committee. The \$18 billion that the lab co-pay is projected to save over 10 years had been earmarked to help pay for increased reimbursement to rural healthcare providers in the Senate's version of the Medicare reform package. Increasing rural health reimbursement is a pet project for Sen. Grassley, who is up for re-election in November 2004. And Grassley's re-election is a big deal for the Republican Party, which holds a slim majority in the Senate.

But Mertz says that in addition to demonstrating the high administrative burden a co-pay would place on labs, ACLA and its members have successfully argued that too much of the burden of paying for proposed increases in rural health reimbursement was being placed on the back of the lab industry. For example, he notes that Medicare Part B lab payments represent only about 2% of total Medicare spending, but a co-pay would have contributed 43% of the funds needed to pay for increased rural health reimbursement.

Meanwhile, the American Association of Bioanalysts (AAB), which represents roughly 1,000 regional independent clinical labs across the nation, has also been active in direct lobbying efforts and has gone hand in hand with ACLA lobbyists to meet with Senate conference staff members. But AAB and its members have also been heavily involved with grass roots efforts to raise awareness among the nation's 41 million Medicare recipients of the threat of a 20% lab co-pay.

In a speech at the recent Lab Institute 2003, October 8-11, AAB lobbyist Bob Waters implored the audience to get involved in the fight against co-pay. "The reason why Congress is taking more than \$18 billion out of your pocket [in the form of the potential lab co-pay] is because you're letting them.... We can win this battle, but it depends upon the strength and intensity of your voices," Waters told the audience.

"We have to fight this one and we have to nail it. And we have to nail it so it doesn't come back again next year and the year after that. [Medicare] members have to understand that this is one of the dumbest ideas that Congress has ever thought up and they don't ever want to go there again," said Waters.

Waters then gave the Lab Institute audience of more than 400 lab presidents, directors, and managers the opportunity to get immediately involved in the lobbying efforts. With the backing of AAB, he organized a bus trip to the Capitol so attendees could visit their Senators' offices and explain their concern about the co-pay. Waters had hoped to attract one bus load of attendees, or about 55 people, for the trip. But more than 120 Lab Institute attendees signed up, so Waters was forced to charter two buses, and still more people took taxi cabs on their own tab for the October 10 trip, which was dubbed the Lab Express.

On the bus ride over to the Capitol, Waters and his staff handed out flyers and lapel

stickers with the "Say No To The Lab Co-Pay" emblem, and gave pointers to the first-time lobbyists on how to approach the staff at their Senators' offices. Then the buses stopped at the sidewalk in front of the Senate buildings, and Lab Institute attendees went to work. Groups of two to seven people visited each of the two Senators from nearly every state.

The highlight of the mission, which was completed within two hours, was the visit to Sen. Grassley's office where a group of four Lab Institute attendees got a private meeting with Grassley's top healthcare policy advisor, Colin Roskey. In the meeting, Julie Loomer, lab billing and coding manager for the University of Iowa Hospitals and Clinics (Iowa City), described the chaos that a lab co-pay would bring on hospital labs. Roskey, who happened to be

carrying the ACLA briefing book on the issue at the time, said that the lab industry's concerns were being heard and understood.

Other successful grass roots efforts organized by AAB have included a direct mail marketing campaign funded by about \$350,000 from member contributions. Bob Birenbaum, administrator of the AAB, says it costs AAB about \$4,000 to mail out 10,000 flyers to



Medicare recipients in a targeted geographic market. The flyers warn seniors that they may soon be required to pay a lab co-pay and provide the name and phone number of their Senator's office so they can call and complain. In addition, many of its member labs are handing out flyers to

Lab Express Attendees On Capitol Hill



Medicare recipients at their patient service centers (PSCs).

Birenbaum adds that some members of AAB have gone above and beyond with additional individual efforts to fight the lab co-pay, including Sunrise Medical Labs (Hauppauge, NY), Westcliff Medical Labs (Newport Beach, CA), Brookside Clinical Lab (Brookhaven, PA), Diagnostic Laboratory Medicine (Bedford, MA), and Kilbourne Medical Lab (Cincinnati). The president of the latter lab, Paul Kilbourne, went as far to stay in Washington for four days after the Lab Institute conference visiting 70 different Senators' offices (including four separate trips to Sen. Grassley's office) to explain the unfairness of the proposed lab co-pay. Kilbourne Medical Lab generates approximately \$10 million per year in revenue, with the majority coming from nursing homes. "A Medicare lab co-pay could drive us out of business," says Kilbourne.

Meanwhile, Larry Siedlick, president of Sunrise Medical Labs, says his company, which derives 28% of its \$40 million in annual revenue from Medicare Part B, has mailed out 20,000 flyers to seniors in New York in addition to providing handouts at its PSCs and contributions to the AAB efforts.

Since Quest and LabCorp have focused their efforts on direct lobbying on Capitol Hill as opposed to more public efforts directed at seniors, some independent lab CEOs had wondered just how hard the national labs were really fighting against the lab co-pay.

Medicare Part B typically represents 30% or more of the total revenue generated by the average independent lab. In contrast, it represents only 13% to 14% of total revenue at Quest and LabCorp. These facts have some independent lab CEOs thinking that maybe the two big commercial labs wouldn't mind seeing the lab co-pay enacted because they'd be better able to withstand the financial hit than their smaller competitors.

LIR posed this question to Pam Sherry, spokeswoman for LabCorp, who responded, "Are we willing to cut off our nose to spite our face? Absolutely not. This is a big issue for LabCorp, and we are doing everything we can to communicate the message in Washington that this is not a good thing for patients or providers."

At a UBS Securities investors' conference in New York City the week of September 22, LabCorp CEO Tom Mac Mahon, laid out what a lab co-pay would do to his company's bottomline. LabCorp generates

about \$375 million, or 13% of its total revenue, from Medicare Part B payments. A 20% co-pay would require it to collect \$75 million from seniors, and roughly half of this figure would be covered by supplemental insurance, according to Mac Mahon. He estimates that about half of the remaining \$37.5 million would need to be written off as bad debt. "How do you tell an 83-year-old person that you're going to ruin their credit if they don't pay?" Mac Mahon asked rhetorically.

Mac Mahon said that while LabCorp has aggressively lobbied against the lab co-pay, smaller independent labs have been even more vociferous. "I've never seen such an outcry. I think it's the small labs that will cause it [the lab co-pay proposal] to fail."

Quest derives approximately 14%, or \$660 million, of its \$4.7 billion in total annual revenue from Medicare Part B. And Quest spokesman Gary Samuels tells *LIR*, "Ken Freeman is spending a huge amount of his time in Washington explaining that the co-pay is a terrible idea for seniors and an administrative burden on labs." "But we've got a limited budget and believe that going

straight to the people making the decision is our best strategy," says Samuels.

"If the lab co-pay were to happen, then, yes, we'd be able to cope with it through better billing systems and bad debt. But I'm amazed that anyone would think this is something we're secretly hoping for," he adds.

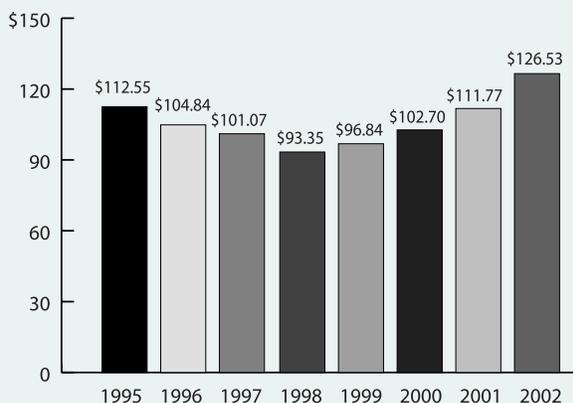
The apparent success at eliminating the co-pay from the reconciled bill suggests that ACLA and the two big commercial labs were working hard behind the scenes. But Mertz says it's not time to celebrate yet. The co-pay could be reintroduced after the reconciled bill reaches the full Congress for further debate.

In addition, Mertz says the reconciled bill could include a freeze on CPI adjustments to the Medicare Part B schedule, including a possible 10-year freeze. Mertz says ACLA has now begun lobbying against this idea. He notes that this year was the first time since 1997 that the lab fee schedule was adjusted for inflation (an increase of 1.1%). Another CPI update is scheduled to automatically go into effect on Jan. 1, 2004, if Congress takes no action to prevent it.

Birenbaum notes that while a lab co-pay would be the most onerous policy, a possible 10-year freeze would also be devastating to independent labs. "The choice between a sudden death through a co-pay, or a long slow death through a long-term freeze is no choice at all," he says. The Clinical Laboratory Coalition has calculated that a long-term freeze would cost laboratories nearly \$10 billion in lost revenue over the next 10 years.

LIR observes Part B lab expenditures totaled \$5.112 billion in calendar-year 2002 and represented just 1.9% of total Medicare spending (including Parts A and B) of \$264.1 billion. Over the past seven years, annual Part B spending per beneficiary has risen by an average of just 1.7% per year to reach \$126.53. 🏠

Average Medicare Part B Spending On Lab Services Per Beneficiary



Source: Centers for Medicare and Medicaid Services

Stanford University Hospital Lab Wins Big IPA Contract

The lab at Stanford University Hospital and Clinics (Stanford, CA) has won a big contract to provide lab test services to Santa Clara County IPA (SCCIPA-San Mateo, CA), a network of 900 physicians and about 112,000 patients in northern California. The contract was formerly held by Quest/Unilab and will be transferred to Stanford effective Jan. 1, 2004.

The contract is capitated and covers clinical lab tests and cytology, but not anatomic pathology. Pricing information was not disclosed. However, Dr. Larry Bonham, president of SCCIPA, told the *Silicon Valley/San Jose Business Journal* that he expected the new contract with Stanford to provide over a million dollars per year in savings. A Quest spokesman would not comment on the contract.

Susie Lu, vice president of clinical lab and pathology services at Stanford University, says the contract represents a big win for Stanford, which is seeking to expand its services to other hospitals and physician offices in northern California. The lab at Stanford, with 400 employees, currently performs about 6.1 million billable tests per year (of which about 5% is from outreach).

In order to serve the new IPA contract, Lu says Stanford will need to open 12 to 15 new patient service centers (PSCs) to supplement its existing five PSCs and expand its courier network. 🏠

Who Will Buy Impath?

Besieged by cash collection and billing management problems, Impath Inc. (New York City) has filed for Chapter 11 bankruptcy reorganization and put itself up for sale. But the question is, "Who will buy it?"

Andreas Dirnagl, healthcare analyst at Harris Nesbitt Gerard (New York City), says obvious potential buyers include Quest Diagnostics and LabCorp. But he believes that the two big commercial labs may be unwilling to make a bid on Impath at any price, given that: 1) its financial statements are unreliable; 2) it is under investigation by the Securities & Exchange Commission; and 3) more than a dozen shareholder lawsuits have been filed against it.

So Dirnagl says Quest, LabCorp, and other lab competitors may simply gain Impath's business by hiring away the company's best pathologists and salespeople. "Impath's biggest assets [i.e., its employees] leave on the elevator every day. If I was Quest or LabCorp, I'd be handing out employment applications on the sidewalk in front of Impath's headquarters," says Dirnagl.

Other buyers could include venture capital firms such as Welsh Carson (New York City), which acquired AmeriPath earlier this year, or perhaps Texas Pacific Partners (Fort Worth), which has a history of investing in troubled healthcare companies.

Impath's bankruptcy filings show estimated assets and debts both top more than \$100 million. Top creditors include Fairport, New-York-based First American Equipment Leasing (\$5.6 million); Manhattan-based Bank Leumi Leasing Corp. (\$793,209); and Albany-based Key Equipment Finance (\$706,306). 🏠

Whistleblower Case Against Quest And LabCorp Moves Ahead

Judge Ronald Buckwalter of the U.S. District Court for the Eastern District of Pennsylvania (Philadelphia) has denied a motion to dismiss a qui tam (*i.e.*, whistleblower) complaint against Quest Diagnostics and LabCorp.

Maria Urbanek is a sales representative for Coastal Clinical Pathology, which is affiliated with Shore Memorial Hospital (Somers Point, NJ), and her lab competes with Quest and LabCorp. Robert Courtney, D.O. is a private practice physician.

The complaint, United States of America Ex Rel. Maria Urbanek and Robert Courtney versus LabCorp and Quest Diagnostics, was initially filed on Sept. 26, 2000 and alleges that the defendants illegally induced lab test referrals for Medicare and Medicaid patients by: 1) providing free gloves, gowns, alcohol swabs, etc; 2) providing free computers and printers; 3) stationing phlebotomists at physician offices; 4) providing “professional courtesy” discounts to doctors and their families; and 5) waiving out-of-network charges to managed care patients referred by physician clients.

Urbanek and Courtney also allege that Quest and LabCorp violated the terms of their Corporate Integrity Agreements (CIAs) with the federal government. In 1996, the defendants entered into separate CIAs with the U.S. Department of Health and Human Services, through the Office of Inspector General (OIG), as part of their settlements of False Claims Act qui tam cases.

The plaintiffs are being represented by Mitch Kreindler from the law firm of Kreindler and Associates (Houston, TX and Philadelphia, PA). Kreindler specializes in whistleblower cases and was involved in several suits brought against the national labs in the mid-1990s that focused on the illegal practice of manipulating test panels in order to obtain higher Medicare and Medicaid reimbursement. Government investigations related to the lab industry resulted in penalties of more than \$1.3 billion between 1995 and 1999.

The primary argument of the Urbanek and Courtney complaint is that when Quest and LabCorp submit claims for payment, they are impliedly certifying that they are in compliance with the Anti-Kickback Statute and Stark law. But, the plaintiffs allege that since the defendants are actually submitting claims for payment without complying with these laws, they are submitting fraudulent claims in violation of the False Claims Act.

Quest and LabCorp had filed a motion to dismiss the case arguing that liability can’t be imposed under the False Claims Act based on an implied false certification of anti-kickback laws or the Stark law. On August 14, 2003, Judge Buckwalter denied this motion to dismiss moving the case toward the discovery phase.

LabCorp has since filed another motion to dismiss, arguing that it is already fighting a competing case in southern California. Meanwhile, Quest spokesman Gary Samuels tells *LIR* that Quest “vigorously denies the allegations.” Samuels notes that the U.S. Department of Justice has reviewed and declined to intervene in the case. He claims that Quest is allowed to provide supplies and services to physician offices as long as they are used exclusively for ordering, transporting, and reporting test results. Quest has gone out of its way to try to ensure that supplies and services given to physician offices are not misused for purposes unrelated to lab testing, according to Samuels. 🏠



Lab Stocks Fall 8%; Quest Initiates Dividend

Stock prices for the 11 companies in the G-2 Laboratory Index fell an unweighted average of 8% in the five weeks ended Oct. 23, 2003, with six stocks falling in price and five rising. So far this year, lab stocks have risen 34%, while the S&P 500 is up 17%, and the Nasdaq is up 41%.

Selected Lab Stocks Ranked by Market Capitalization (\$ millions)

Quest Diagnostics	\$7,095
LabCorp	4,767
Myriad Genetics	343
LabOne	287
Specialty Labs	283
Bio-Reference	160
Medtox Scientific	31

Source: LIR

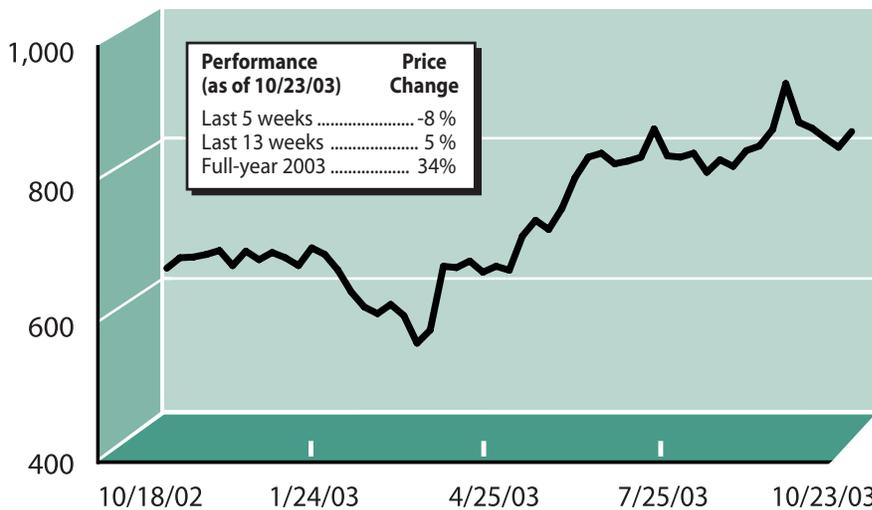
Quest Diagnostics (Teterboro, NJ) was up 5% to \$67.46 per share. The company was buoyed by news that a 20% lab co-pay was unlikely to be part of the reconciled Medicare reform package that will go to Congress (see page 1). In addition, Quest recently announced that it will begin paying a quarterly dividend of \$0.15 per share, an amount that equates to a 1% annual dividend yield.

Other stocks moving up included **LabCorp** (Burlington, NC), which climbed 7% to \$32.91 per share; **Bio-Reference Labs** (Elmwood Park, NJ),

which was up 27% to \$13.99 per share; and **Medtox Scientific** (St. Paul, MN), up 19% to \$6.23 per share.

Meanwhile, **PharmChem** (Haltom City, TX) plunged 60% to \$0.32 per share on news that it had lost a major customer and as a result may have to pursue "significant" cost reductions, including layoffs. The Administrative Office of U.S. Courts, which had contracted with PharmChem for nearly 15 years for drug-testing services, has switched to three other labs, PharmChem said. Revenue from the AOUSC contract totaled about \$5.8 million, or 28% of PharmChem's sales, for the first nine months of this year. 🏠

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, 5 weeks ended 10/23/03

UP	Price	% Chg
Bio-Reference	13.99	27
LabCorp	32.91	7
MDS	15.09	10
Medtox	6.23	19
Quest	67.46	5
DOWN		
Enzo Biochem	19.28	-12
Impath	2.15	-48
LabOne	24.43	-2
Myriad	12.66	-1
PharmChem	0.33	-60
Specialty	12.68	-6

INDUSTRY *buzz*

If you think the commercial labs have gotten too big and now wield too much market clout, then take a look at the managed care industry.

On October 27, Anthem Inc. (Indianapolis, IN) announced plans to acquire WellPoint Health Networks (Thousand Oaks, CA) for \$16 billion. Assuming the deal passes potential antitrust issues that could be raised by the Federal Trade Commission, Anthem/WellPoint will cover 26 million health plan lives across the country and generate \$36 billion in annual revenue.

On the same day, United HealthGroup (Minneapolis, MN) agreed to buy Mid Atlantic Medical Services Inc. (MAMSI—Rockville, MD) for \$3 billion. Together, United and MAMSI will cover more than 3.5 million people in the mid-Atlantic region and 19 million nationwide.

Over the past five years hospitals, physician groups, drug companies, and labs have been consolidating, gaining the ability to charge higher fees to health insurance companies (or at least stem the downward reimbursement spiral of the mid-1990s).

Now health insurance companies, which have been raising premiums to counter higher costs, are regaining leverage. The two recently announced deals may result in a shift in the balance of power back toward health insurers and away from providers. And the combination of bigger health insurance companies and the strong desire on the part of employers to stem double-digit premium hikes could lead to a renewed round of reimbursement pressure for labs and other providers. 🏠

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LabCorp 336-584-5171

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Quest Diagnostics 201-393-5000

Stanford University Hospital and
Clinics 650-723-4000

Sunrise Medical Labs 800-782-0282

The Lab at Steamboat 970-879-8468

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