



Outlook for Medicare Laboratory Payment Policy

October 2025

Capstone at a glance

Areas of focus

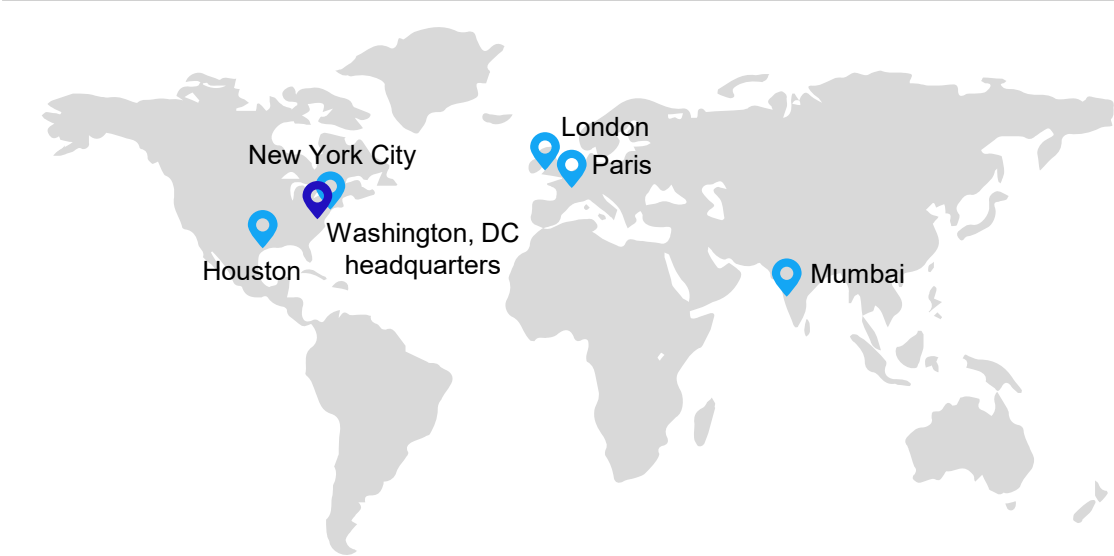
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Executive Summary (I/II)

The Bottom Line

- Capstone assigns a 65% probability that Congress will delay Medicare payment cuts to the clinical laboratory fee schedule (CLFS) for another year before 2026.
- We believe investors (and some in the media) misinterpret changes to the Congressional Budget Office (CBO) methodology related to commercial lab rates and thus underappreciate the probability of further delay.
- Ultimately, we believe another one-year delay to cuts imposed by the Protecting Access to Medicare Act (PAMA) will either continue to save the federal government money or be budget-neutral. We do not believe the delay will cost money. As such, we believe Congress will do what it has done five times before and delay the scheduled cuts for another year.
- A delay in payment cuts will benefit clinical laboratories, including Labcorp Holdings Inc. (LH) and Quest Diagnostics Inc. (DGX).
- Labcorp expects a \$100M impact to both the top line and bottom line in 2026 if the cuts are not delayed. The company notes it believes it can offset roughly \$25M of that impact. Quest similarly expects a \$100M impact in 2026 if the cuts are not delayed. The company believes it can offset some of that impact.

Capstone's Call at a Glance

Capstone's Prediction: 65% probability that Congress delays Medicare laboratory cuts before 2026.

Companies Impacted: Labcorp Holdings Inc. (LH) and Quest Diagnostics Inc. (DGX)

Potential Impact: Both Labcorp and Quest expect up to a \$100M headwind in 2026 if cuts are not delayed.

Executive Summary (II/II)

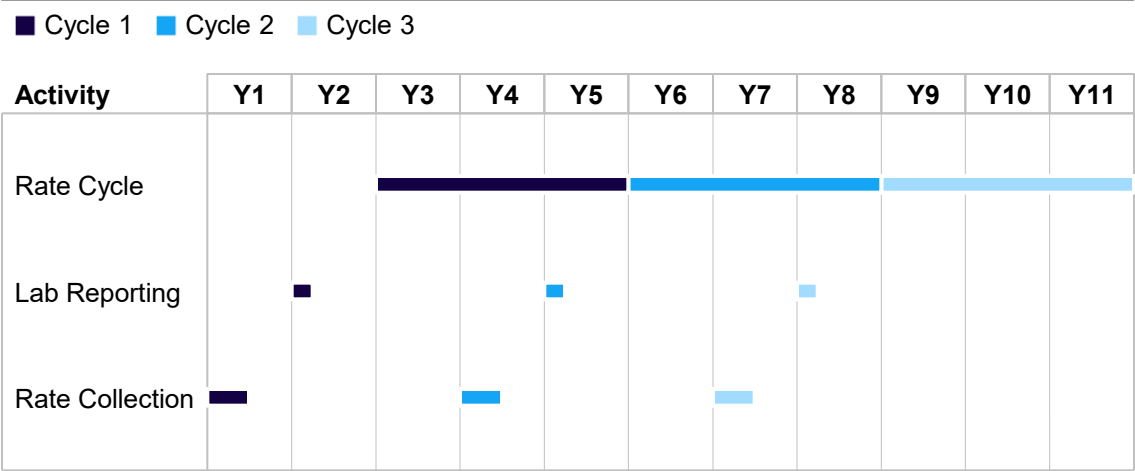
- **Background:** The Protecting Access to Medicare Act of 2014 (PAMA) updated the Medicare payment methodology for clinical diagnostic lab tests (CDLT) within the clinical laboratory fee schedule (CLFS). The law tied Medicare rates to commercial market rates. Because Medicare rates at the time were higher than commercial rates, the “tying” would be felt by industry stakeholders as a cut to Medicare reimbursement. The law established year-over-year limits on the severity of cuts to Medicare rates. Since 2020, Congress has intervened five times to prevent a cut as large as 15% in the following year. Without congressional intervention by the end of 2025, cuts are scheduled to take place in 2026.
- **Delay-to-save:** The Congressional Budget Office (CBO) has scored each of the five pieces of legislation delaying cuts as saving the government money. Because delays save money, it is far easier for Congress to include such provisions in end-of-year legislative vehicles. While counterintuitive, we believe CBO’s logic relies on three assumptions:
 - 1) In the year where cuts are delayed, the government loses money versus the CBO baseline.
 - 2) In the second and third years following the delay, the government saves money as hospital-based labs (with higher 2019 commercial rates) are supposed to be incorporated into the payment methodology but are delayed.
 - 3) In the fifth, sixth, and seventh years following the delay, the government saves a considerable amount of money as recent commercial rate data are supposed to be incorporated into the methodology but are delayed.
- **Capstone’s Argument:** CBO’s third assumption underwent some revision earlier this year, which Laboratory Economics reported in Spring 2025. CBO also noted the change in January 2025, explaining that it “reduced its projections of growth in the amounts that Medicare pays to clinical laboratories to better reflect the amounts that Medicare has paid in recent years.” However, we believe investors are misinterpreting CBO.
 - We believe CBO is suggesting that the growth in commercial rates has slowed or is lower than its assumed growth rate (CPI-U). But that is not enough to believe that another delay will cost the government money. For that to be true, CBO would have to believe that commercial rates are *declining*. We do not believe that is what CBO is suggesting, and as such, the third CBO assumption likely still holds, and the delay saves money. Because we believe a delay in cuts saves money, we believe Congress will act for a sixth time to delay these cuts.
- **Risks to our thesis:** We could misinterpret CBO, and if the delay costs money, we believe it is far less likely to be included in an end-of-year spending package. Further, Congress could fail to enact any legislation that a delay could ride on.
- **Unpacking our probability:** Congress has acted five times in the last eight years (62.5%) to delay lab cuts, including each of the last five years (100%). We discount this 100% figure by 35 percentage points to reflect 1) the risk of inaction generally caused by political infighting and the government shutdown, and 2) the potential for CBO to score the delay as costing money and thus reducing congressional willingness to act.

The Protecting Access to Medicare Act (PAMA) updated the Medicare payment methodology for clinical diagnostic lab tests (CDLT), tying Medicare rates to the commercial market

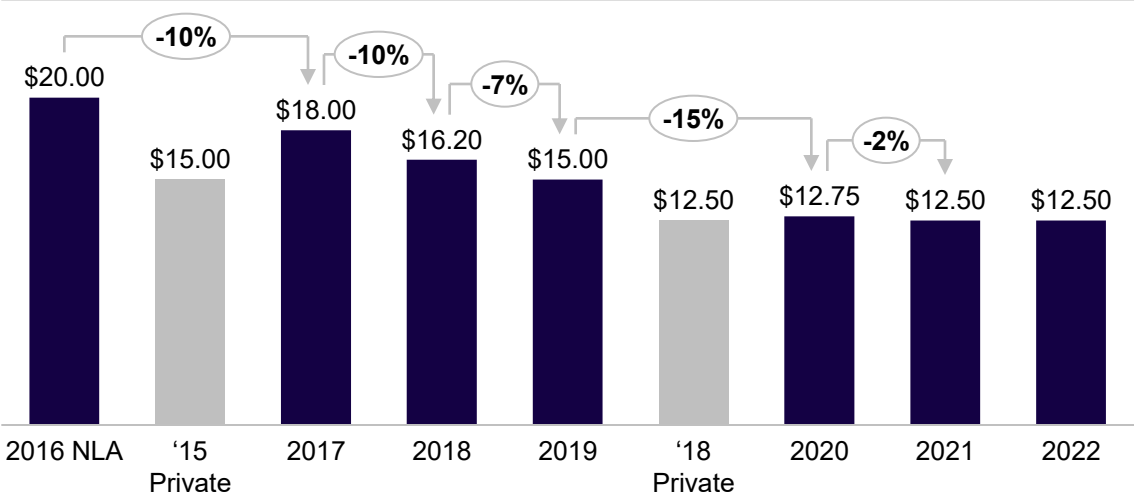
Lab Test Reimbursement Overview

- PAMA Overview:** The Protecting Access to Medicare Act of 2014 (PAMA) required CMS to update the payment methodology for clinical diagnostic lab tests (CDLTs) under the Clinical Laboratory Fee Schedule (CLFS).
- Pre-PAMA Reimbursement:** Prior to PAMA, Medicare reimbursed lab tests under the CLFS – a collection of 57 fee schedules set by Medicare Administrative Contractors (MACs) – which was established in 1984. Base rates were stagnant, besides CPI-U adjustments, except to establish reimbursement for new tests, or make statutory, across-the-board updates.
 - National Limitation Amount (NLA):** To contain lab test costs, Medicare established an NLA, capping rates for each test. Medicare would pay the lesser of 1) lab charges, 2) jurisdiction’s payment rate, or 3) the NLA – 74% of the median rate for each lab test across the 57 fee schedules.
 - NLA Utilization:** In 2000, ~84% of payment amounts were set at the NLA, eliminating geographic variation and set a national rate per test.
- PAMA Changes:** Because rates were not adjusted and based on local lab rates for 1984 and 1985, Medicare was actually paying more for lab tests than commercial payors. PAMA was designed to update the CLFS and lower reimbursement to competitive, market-based lab test prices.
 - Methodology Change:** Medicare updates the CLFS by collecting data of rates paid by private payors and using the weighted average of those rates to set a new payment rate. Statutorily, rates are required to be updated every three years using data reported by labs⁽¹⁾.
 - Rate Cut Phase-In:** For the first three years, cuts would be capped at 10%. The following three years, cuts would be capped at 15%.

PAMA Collection, Reporting, and Rate Cycle



Phase-In Rate Reduction Example



Notes: (1) PAMA originally defined applicable laboratories by having a majority of Medicare revenue paid under the CLFS. In the 2019 Medicare Physician Fee Schedule CMS changed this to include more hospital labs – which would increase the weighted average commercial rate, reducing cut impact | Source: CMS, OIG, Capstone analysis

Congress has repeatedly delayed PAMA, as CBO scoring of delays supports savings; delays have been more feasible to preserve lab rates than passing SALSA – which increases spend

Significant Federal Policy Modifying Clinical Lab Medicare Reimbursement

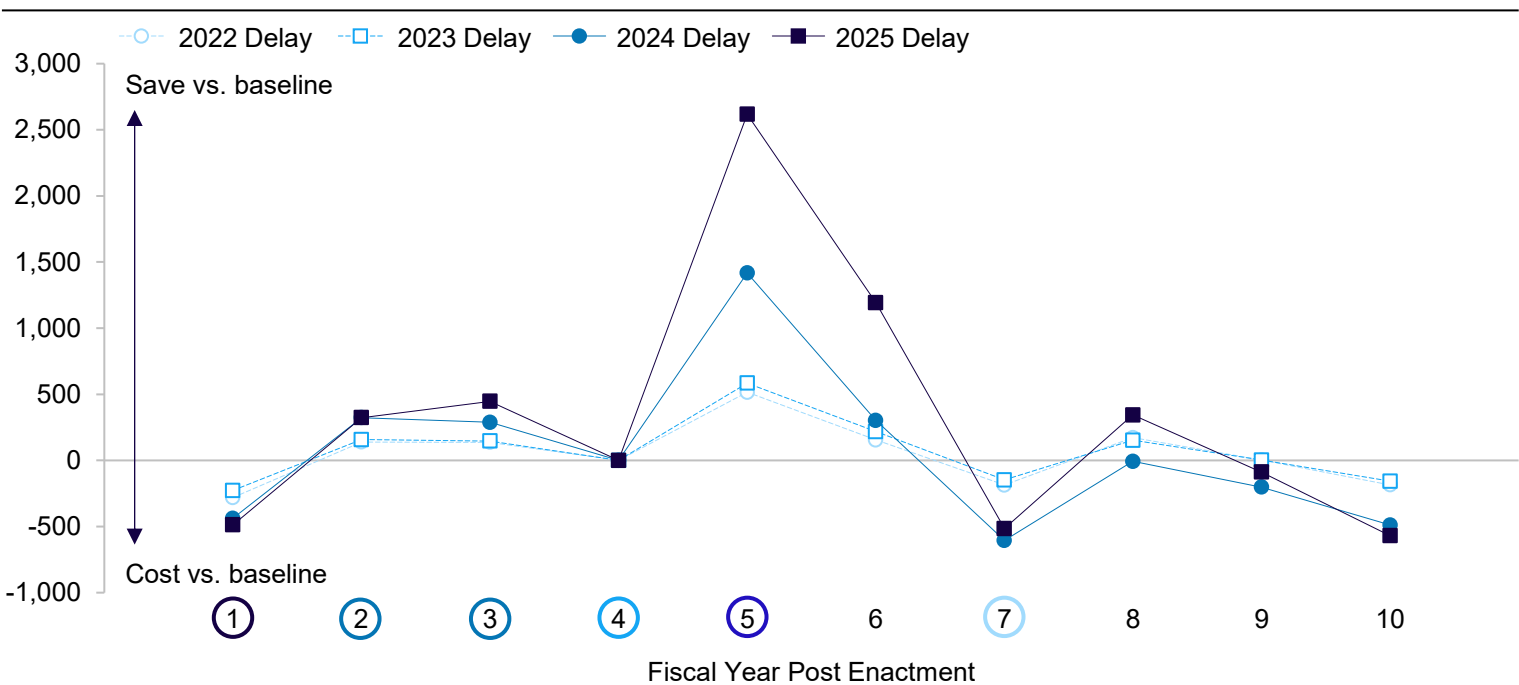
Law / Reg	Enacted	Description	CBO 10yr Savings Est. (\$M)
Protecting Access to Medicare Act (PAMA)	Dec. 2014	Changed Medicare reimbursement policy for clinical diagnostic laboratory tests (CDLTs) under the clinical laboratory fee schedule (CLFS).	2,500
CMS Regulatory Action	Jun. 2016	Delayed PAMA implementation until Jan. 1, 2018. PAMA was originally designed to take effect on Jan. 1, 2017.	Score Unavailable ¹
Further Consolidated Appropriations Act	Dec. 2019	Codified CMS regulation. Delayed second round of private rate reporting one year (2021 instead of 2020). Did not adjust reimbursement cut limit / cap.	0
CARES Act	Mar. 2020	Delayed the second round of private rate reporting one year (to 2022 from 2021) and set the 2021 reimbursement cut limit to 0% in 2021 (preventing the max 15% cut).	Score Unavailable
Protecting Medicare and American Farmers from Sequester Cuts Act	Dec. 2021	Delayed the second round of private rate reporting one year (to 2023 from 2022) and set the reimbursement cut limit to 0% in 2022 (preventing the max 15% cut).	470
Consolidated Appropriations Act	Dec. 2022	Delayed the second round of private rate reporting one year (to 2024 from 2023) and set the reimbursement cut limit to 0% in 2023 (preventing the max 15% cut).	731
Further Continuing Appropriations and Other Extensions Act	Nov. 2023	Delayed the second round of private rate reporting one year (to 2025 from 2024) and set the reimbursement cut limit to 0% in 2024 (preventing the max 15% cut).	589
Continuing Appropriations and Extensions Act	Sep. 2024	Delayed the second round of private rate reporting one year (to 2026 from 2025) and set the reimbursement cut limit to 0% in 2025 (preventing the max 15% cut).	3,264

Delays have limited total cuts to date by adding 0% cut years, but CBO scores the delay as saving federal money by postponing the introduction of new commercial rates

Law / Reg	Enacted	CBO Score ¹	Metric	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Protecting Access to Medicare Act (PAMA) Original Law	12/16/14	\$2,500M	Collection Period	2015	2015	2015	2018	2018	2018	2021	2021	2021	2024	2024	2024	2027	2027	2027	2030	2030	2030
			Reporting Period	2016	2016	2016	2019	2019	2019	2022	2022	2022	2025	2025	2025	2028	2028	2028	2031	2031	2031
			New Rate	✓			✓			✓			✓			✓			✓		
			Reimb. Cut Limit	10%	10%	10%	15%	15%	15%	-	-	-	-	-	-	-	-	-	-	-	-
CMS Regulatory Action CMS Modification	6/23/16	N/A	Collection Period		2016	2016	2016	2019	2019	2019	2022	2022	2022	2025	2025	2025	2028	2028	2028	2031	2031
			Reporting Period		2017	2017	2017	2020	2020	2020	2023	2023	2023	2026	2026	2026	2029	2029	2029	2032	2032
			New Rate		✓			✓			✓			✓			✓			✓	
			Reimb. Cut Limit		10%	10%	10%	15%	15%	15%	-	-	-	-	-	-	-	-	-	-	-
Further Consolidated Appropriations Act	12/20/19	\$0	Collection Period		2016	2016	2016	2016	2019	2019	2019	2023	2023	2023	2026	2026	2026	2029	2029	2029	2032
			Reporting Period		2017	2017	2017	2017	2021	2021	2021	2024	2024	2024	2027	2027	2027	2030	2030	2030	2033
			New Rate		✓				✓			✓			✓			✓			✓
			Reimb. Cut Limit		10%	10%	10%	15%	15%	15%	-	-	-	-	-	-	-	-	-	-	-
CARES Act	3/27/20	N/A	Collection Period		2016	2016	2016	2016	2016	2019	2019	2019	2024	2024	2024	2027	2027	2027	2030	2030	2030
			Reporting Period		2017	2017	2017	2017	2017	2022	2022	2022	2025	2025	2025	2028	2028	2028	2031	2031	2031
			New Rate		✓					✓			✓			✓			✓		
			Reimb. Cut Limit		10%	10%	10%	0%	15%	15%	15%	-	-	-	-	-	-	-	-	-	-
Protecting Medicare and American Farmers from Sequester Cuts Act	12/10/21	\$470M	Collection Period		2016	2016	2016	2016	2016	2016	2019	2019	2019	2025	2025	2025	2028	2028	2028	2031	2031
			Reporting Period		2017	2017	2017	2017	2017	2017	2023	2023	2023	2026	2026	2026	2029	2029	2029	2032	2032
			New Rate		✓						✓			✓			✓			✓	
			Reimb. Cut Limit		10%	10%	10%	0%	0%	15%	15%	15%	-	-	-	-	-	-	-	-	-
Consolidated Appropriations Act	12/29/22	\$731M	Collection Period		2016	2016	2016	2016	2016	2016	2016	2019	2019	2019	2026	2026	2026	2029	2029	2029	2032
			Reporting Period		2017	2017	2017	2017	2017	2017	2017	2024	2024	2024	2027	2027	2027	2030	2030	2030	2033
			New Rate		✓						✓			✓			✓			✓	
			Reimb. Cut Limit		10%	10%	10%	0%	0%	0%	15%	15%	15%	-	-	-	-	-	-	-	-
Further Continuing Appropriations and Other Extensions Act	11/16/23	\$589M	Collection Period		2016	2016	2016	2016	2016	2016	2016	2016	2019	2019	2019	2027	2027	2027	2030	2030	2030
			Reporting Period		2017	2017	2017	2017	2017	2017	2017	2017	2025	2025	2025	2028	2028	2028	2031	2031	2031
			New Rate		✓								✓			✓			✓		
			Reimb. Cut Limit		10%	10%	10%	0%	0%	0%	0%	15%	15%	15%	-	-	-	-	-	-	-
Continuing Appropriations and Extensions Act Current Law	9/26/24	\$3,264M	Collection Period		2016	2016	2016	2016	2016	2016	2016	2016	2016	2019	2019	2019	2028	2028	2028	2031	2031
			Reporting Period		2017	2017	2017	2017	2017	2017	2017	2017	2017	2026	2026	2026	2029	2029	2029	2032	2032
			New Rate		✓									✓			✓			✓	
			Reimb. Cut Limit		10%	10%	10%	0%	0%	0%	0%	0%	15%	15%	15%	-	-	-	-	-	-

CBO scored savings have increased each time Congress delays cuts; however, the basic methodology likely still holds, in our opinion

CBO Scored Savings¹ of Previous PAMA Delay Legislation, \$M (normalized by year post enactment)



Commentary on CBO Methodology

- 1 In year 1, the government loses money. There was supposed to be a cut to Medicare rates of up to 15%, but with no cut implemented, it costs money.
- 2/3 In years 2 and 3, hospital-based labs are incorporated into the payment methodology. Hospital-based labs are expected to have higher commercial rates, reducing the magnitude of Medicare cuts. That costs money. However, because the introduction of those rates is delayed by a year, the CBO scores those years as saving money.
- 4 In year 4, the only change from delay is reimposition of a 15% rate cut limit. If CBO believes Medicare rates will already approximate commercial rates, then the delay saves no money (it doesn't cost money either).
- 5 In year 5, new commercial rates are used for Medicare rate setting. If CBO believes commercial rates in, for example, 2027 are higher than 2019, then delaying this change generates savings. For it to cost money, rates must have declined.
- 7 In year 7, the only change is using commercial rates one year in the future compared to the delay scenario. Higher commercial rates cause higher Medicare rates, which costs money.

Law / Reg	Metric	Y0	①	②	③	④	⑤	6	⑦	8	9	10
Previous Law (CBO Baseline)	Collection Period	2016	2016	2019	2019	2019	2027	2027	2027	2030	2030	2030
	Reporting Period	2017	2017	2025	2025	2025	2028	2028	2028	2031	2031	2031
	New Rate			✓			✓			✓		
	Reimb. Cut Limit	0%	15%	15%	15%	-	-	-	-	-	-	-
Hypothetical 2025 Delay	Collection Period	2016	2016	2016	2019	2019	2019	2028	2028	2028	2031	2031
	Reporting Period	2017	2017	2017	2026	2026	2026	2029	2029	2029	2032	2032
	New Rate				✓			✓			✓	
	Reimb. Cut Limit	0%	0%	15%	15%	15%	-	-	-	-	-	-

Note: (1) Positive numbers indicate federal savings, negative numbers indicate federal costs. All figures are scored relative to CBO's baseline before the legislation is enacted.

Source: Congress.gov, CBO, Capstone analysis

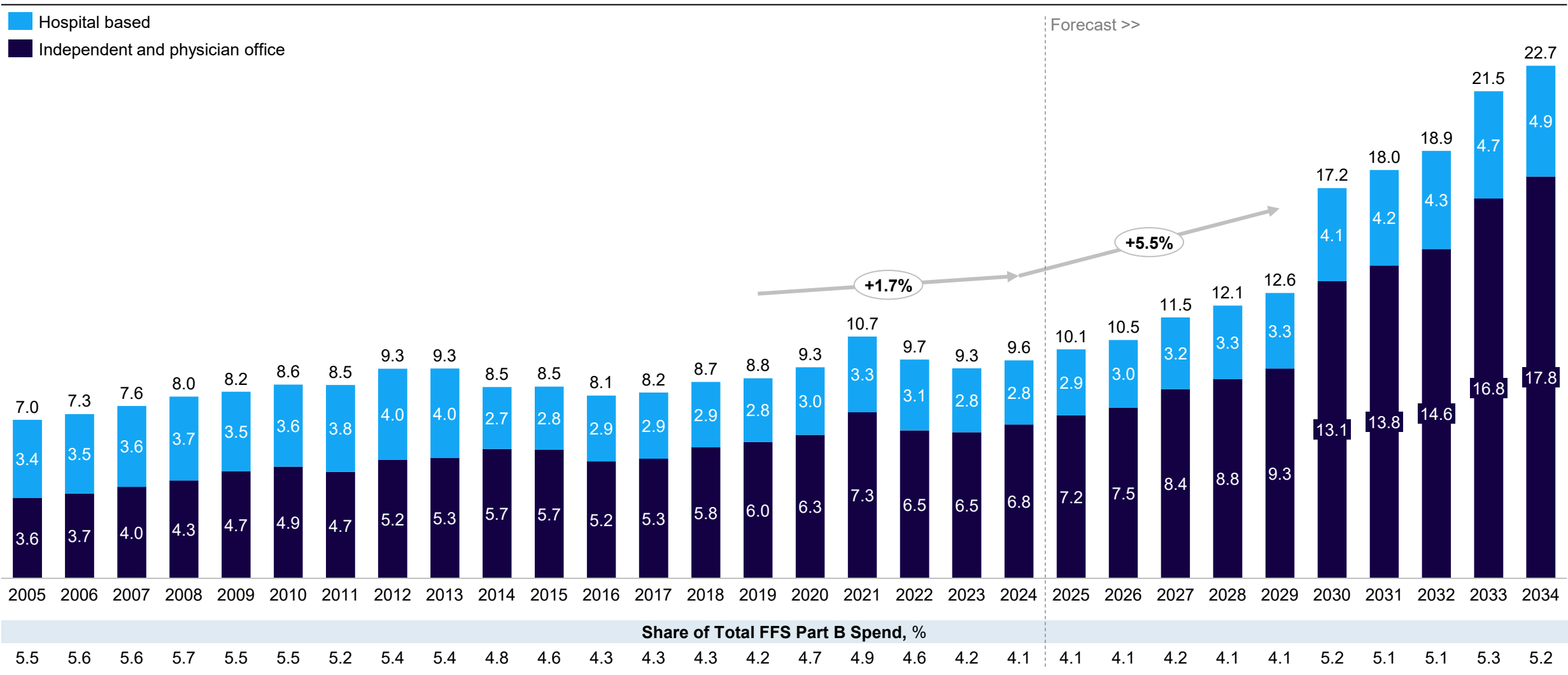
Medicare Trustee projections over time similarly demonstrate CBO’s core methodology, showing how a delay saves federal dollars by moving spend increases out one year

Medicare Trustees Actual and Forecast Y/Y % Change in Medicare FFS Expenditures on Lab Tests

										Actual Prediction		<0%	0%-5%	5%-10%	10%-15%	15%-20%	20%-25%	25%<
Proj. Year	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
2018	3%	-6%	-3%	-1%	14%	7%	6%	15%	6%	6%	14%							
2019	2%	3%	-6%	-2%	13%	6%	6%	15%	6%	6%	14%	9%						
2020	2%	6%	2%	-8%	6%	9%	6%	8%	15%	6%	8%	11%	5%					
2021	2%	6%	2%	4%	4%	-9%	7%	4%	5%	19%	5%	5%	12%	5%				
2022 ¹	2%	6%	2%	5%	10%	-8%	-1%	N/A	2%	5%	22%	5%	5%	12%	5%			
2023	2%	6%	2%	6%	14%	-7%	3%	3%	10%	5%	5%	33%	5%	5%	12%	5%		
2024	2%	6%	2%	6%	14%	-8%	-8%	1%	3%	10%	5%	5%	33%	5%	5%	14%	5%	
2025	2%	6%	2%	5%	15%	-10%	-4%	4%	5%	4%	9%	5%	5%	37%	5%	5%	14%	5%

Medicare FFS spending on lab tests grew ~1.7% per annum from 2019 to 2024; Medicare Trustees expect expenditures to grow ~5.5% per annum through 2029

Medicare FFS Part B Expenditures on Lab Tests, \$B (incurred basis)



Source: Medicare Trustees, MedPAC, Capstone analysis

Per capita Medicare FFS spending on lab tests grew ~5.2% per annum from 2019 to 2024; Medicare Trustees expect per capita expenditures to grow ~5.5% per annum through 2029

Per Capita Medicare FFS Part B Expenditures on Lab Tests, \$ per Part B FFS Beneficiary

