AMERIPATH INC
Form 10-Q
May 15, 2002

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2002

or

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

Commission File Number: 000-22313

AMERIPATH, INC.

(Exact name of registrant as specified in its charter)

Delaware	65-0642485
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7289 Garden Road, Suite 200, Riviera Beach, Florida	33404
(Address of principal executive offices)	(Zip Code)

(561) 845-1850

(Registrant's telephone number, including area code)

Not Applicable

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [_]

The registrant had 30,497,159 shares of common stock, $.01 par value, outstanding as of May 7, 2002.

AMERIPATH, INC. AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

AMERIPATH, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)

ASSETS	March 31, 2002 (Unaudited)	December 31, 2001
CURRENT ASSETS:		
Cash and cash equivalents	$ 1,051	$ 4,808
Accounts receivable, net	85,878	81,595
Inventories	2,153	1,892
Other current assets	16,196	15,780
Total current assets	105,278	104,075

PROPERTY AND EQUIPMENT, NET	24,215	24,118
OTHER ASSETS:		
Goodwill, net	237,568	216,222
Identifiable intangibles, net	257,085	253,562
Other	6,734	6,485
Total other assets	501,387	476,269
TOTAL ASSETS	$ 630,880	$ 604,462
LIABILITIES AND COMMON STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	$ 44,002	$ 42,876
Current portion of long-term debt	663	469
Other current liabilities	3,712	3,910
Total current liabilities	48,377	47,255
LONG-TERM LIABILITIES:		
Revolving loan	97,000	90,000
Long-term debt	2,786	2,853
Other liabilities	2,289	2,690
Deferred tax liability	64,814	62,474
Total liabilities	166,889	158,017
COMMITMENTS AND CONTINGENCIES		
COMMON STOCKHOLDERS' EQUITY:		
Common stock	305	302
Additional paid-in capital	317,941	314,168
Retained earnings	97,368	84,720
Total common stockholders' equity	415,614	399,190
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 630,880	$ 604,462

The accompanying notes are an integral part of these unaudited financial statements.

AMERIPATH, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share amounts)
(Unaudited)

Three Months Ended

	March 31,	
	2002	2001
NET REVENUES:		
Net patient service revenue	$ 105,802	$ 91,724
Net management service revenue	7,090	7,021
Total net revenues	112,892	98,745
OPERATING COSTS AND EXPENSES:		
Cost of services	54,340	48,432
Selling, general and administrative expenses	20,049	17,218
Provision for doubtful accounts	13,674	10,658
Amortization expense	2,782	4,526
Merger- related charges	--	7,103
Total operating costs and expenses	90,845	87,937
INCOME FROM OPERATIONS	22,047	10,808
OTHER INCOME (EXPENSE):		
Interest expense	(1,053)	(4,742)
Other, net	85	24
Total other expense	(968)	(4,718)
INCOME BEFORE INCOME TAXES	21,079	6,090
PROVISION FOR INCOME TAXES	8,431	2,849
NET INCOME	$ 12,648	$ 3,241
BASIC EARNINGS PER COMMON SHARE:		
Basic earnings per common share	$ 0.42	$ 0.13
Basic weighted average shares outstanding	30,325	24,809
DILUTED EARNINGS PER COMMON SHARE:		
Diluted earnings per common share	$ 0.41	$ 0.12
Diluted weighted average shares outstanding	31,228	25,983

The accompanying notes are an integral part of these unaudited financial statements.

AMERIPATH, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three M Ma
	2002
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net income	$ 12,648
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization	4,683
Loss on disposal of assets	(15)
Deferred income taxes	(2,000)
Provision for doubtful accounts	13,674
Merger-related charges	--
Changes in assets and liabilities (net of effects of acquisitions):	
Increase in accounts receivable	(17,957)
Increase in inventories	(261)
(Increase) / decrease in other current assets	(416)
Increase in other assets	(70)
Increase in accounts payable and accrued expenses	3,279
Pooling merger-related charges paid	(68)
Net cash provided by operating activities	13,497
CASH FLOWS FROM INVESTING ACTIVITIES:	
Acquisition of property and equipment	(1,684)
Merger-related charges paid	(662)
Cash paid for acquisitions and acquisition costs, net of cash acquired	(6,893)
Payments of contingent notes	(17,653)
Net cash used in investing activities	(26,892)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Proceeds from exercise of stock options and warrants	735
Debt issuance costs	(206)
Principal payments on long-term debt	(109)
Net borrowings under revolving loan	7,000
Tax benefits from stock options	2,218
Net cash provided by financing activities	9,638
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(3,757)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	4,808
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 1,051
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:	
Contingent stock issued	$ 822

The accompanying notes are an integral part of these unaudited financial statements.

AMERIPATH, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements, which include the accounts of AmeriPath, Inc. and its Subsidiaries (collectively, "AmeriPath" or the "Company"), have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial reporting and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the financial statements do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, such interim financial statements contain all adjustments (consisting of normal recurring items) considered necessary for a fair presentation of the Company's financial position, results of operations and cash flows for the interim periods presented. The results of operations and cash flows for any interim periods are not necessarily indicative of results which may be reported for the year ended December 31, 2002.

The accompanying unaudited interim financial statements should be read in conjunction with the audited consolidated financial statements, and the notes thereto, included in the Company's Annual Report on Form 10-K for the year ended December 31, 2001, as filed with the Securities and Exchange Commission.

In order to maintain consistency and comparability between periods presented, certain amounts have been reclassified in order to conform with the financial statement presentation of the current period.

RECENT ACCOUNTING PRONOUNCEMENTS

In June 1998, the FASB issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," ("SFAS 133") and in June 1999, the FASB issued Statement of Financial Accounting Standards No. 137 "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB Statement No. 133," which delayed the effective date the Company is required to adopt SFAS 133 until its fiscal year 2001. In June 2000, the FASB issued Statement of Financial Accounting Standards No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities - an Amendment to FASB Statement No. 133." This statement amended certain provisions of SFAS 133 which requires the Company to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value will be immediately recognized in earnings. The Company does not enter into derivative financial instruments for trading purposes.

AMERIPATH, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"). SFAS 141 requires the purchase method of accounting for business combinations initiated after June 30, 2001 and eliminates the pooling-of-interests method. The Company does not believe that the adoption of SFAS 141 will have a significant impact on its financial statements.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), which is effective January 1, 2002. SFAS 142 requires, among other things, the discontinuance of goodwill amortization. In addition, the standard includes provisions for the reclassification of certain existing recognized intangibles as goodwill, reassessment of the useful lives of existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the identification of reporting units for purposes of assessing potential future impairments of goodwill. SFAS 142 also requires us to complete a transitional goodwill impairment test six months from the date of adoption. We are currently assessing, but have not yet determined, the impact of SFAS 142 on our financial position and results of operations. For the first quarter of 2001 and for the year ending December 31, 2001, goodwill amortization was approximately $1.7 million and $7.4 million, respectively. Based on our preliminary assessment of SFAS 142, The Company has stopped amortizing goodwill effective January 1, 2002. In addition, due to the fact that a portion of this goodwill was not tax deductible, our effective tax rate was greater than the statutory rate. The elimination of the goodwill amortization, including nondeductible goodwill amortization, from future periods should result in a 1% to 2% reduction in our effective tax rate.

In July 2001, the FASB issued SFAS, No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. It applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development, and (or) the normal operation of a long-lived asset, except for certain obligations of lessees. The provisions of SFAS 143 will be effective for fiscal years beginning after June 15, 2002; however early application is permitted. The Company is currently evaluating the implications of adoption of SFAS 143 on its financial statements.

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 provides accounting guidance for financial accounting and reporting for impairment or disposal of long-lived assets. SFAS 144 supersedes SFAS 121. SFAS 144 is effective for the Company in fiscal 2002. Management does not currently believe that the implementation of SFAS 144 will have a material impact on the Company's financial condition or results of operations.

NOTE 2 -- ACQUISITIONS

During the first quarter of 2002, the Company acquired an operation which was previously managed under a management services agreement. Total consideration paid consisted of cash, consideration in the form of contingents notes and the assumption of certain liabilities. In addition, during the first quarter of 2002, we made contingent note payments of $17.7 million relating to previous acquisitions.

AMERIPATH, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -
(Continued)

NOTE 3 - INTANGIBLE ASSETS

Intangible assets and the related accumulated amortization and amortization periods are set forth below (dollars in thousands):

	March 31, 2002	December 31, 2001	March 31, 200 Amortization Per (Years) Range	We A
Hospital contracts	$ 215,944	$ 211,638	25-40	
Physician client lists	68,645	66,646	10-30	
Laboratory contracts	4,543	4,543	10	
Management service agreement	11,379	11,379	25	
	300,511	294,206		
Accumulated amortization	(43,426)	(40,644)		
Identifiable intangibles, net	$ 257,085	$ 253,562		
Goodwill	$ 260,707	$ 239,361		
Accumulated amortization	(23,139)	(23,139)		
Goodwill, net	$ 237,568	$ 216,222		

The weighted average amortization period for identifiable intangible assets is approximately 27 years.

NOTE 4 - MERGER-RELATED CHARGES

In connection with the Inform DX merger and other previous acquisitions, the Company has recorded reserves for transaction costs, employee-related costs (including severance agreement payouts) and various exit costs associated with the consolidation of certain operations, including the elimination of duplicate facilities and certain exit and restructuring costs. As part of the Inform DX acquisition, the Company is closing or consolidating certain facilities.

A reconciliation of the activity for the quarter ended March 31, 2002 with respect to the merger-related reserves is as follows:

	Balance December 31, 2001	Statement of Operations Charges	Payments	B Mar
Transaction costs	$ 116	$ --	$(68)	$
Employee termination costs	3,432	--	(401)	

Lease commitments	2,165	--	(235)
Other exit costs	160	--	(26)
Total	5,873	$ --	$ (730)
Less: portion included in other current liabilities	(3,183)		
Total included in other liabilities	$2,690		

AMERIPATH, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

NOTE 5 - MARKETABLE SECURITIES

The Company accounts for investments in certain debt and equity securities under the provisions of Statement of Financial Accounting Standards No. 115 ("SFAS No. 115"), "Accounting for Certain Debt and Equity Securities". Under SFAS No. 115, the Company must classify its debt and marketable equity securities in one of three categories: trading, available-for-sale, or held-to-maturity.

In September 2000, the Company made a $1 million investment in Genomics Collaborative, Inc ("GCI") for which it received 333,333 shares of Series D Preferred Stock, par value $0.01. The shares of GCI Series D Preferred Stock are convertible into shares of GCI common stock on a one-for-one basis and are redeemable after 2005 at $3.00 per share at the option of the holder. GCI is a privately held, start-up, company which has a history of operating losses. As of March 31, 2002, it appears that GCI has sufficient cash to fund operations for the next twelve months. In the event that they are unable to become profitable and/or raise additional funding, it could result in an impairment of the Company's investment. This available for sale security is recorded at its estimated fair value, which approximates cost, and is classified as other assets on the Company's consolidated balance sheet. At March 31, 2002, there were no unrealized gains or losses associated with this investment.

NOTE 6 - COMMITMENTS AND CONTINGENCIES

Liability Insurance -- The Company is insured with respect to general liability on an occurrence basis and medical malpractice risks on a claims made basis. The Company records an estimate of its liabilities for claims incurred but not reported. Such liabilities are not discounted. Effective July 1, 1999, the Company changed its medical malpractice carrier and the Company is currently in a dispute with its former insurance carrier on an issue related to the applicability of surplus insurance coverage. The Company believes that an unfavorable resolution, if any, of such dispute would not have a material adverse effect on the Company's financial position or results of operations.

The Company was recently notified by its medical malpractice carrier that they will no longer be underwriting medical malpractice insurance and this has placed the Company on non-renewal status effective July 1, 2002. The Company is currently evaluating other potential carriers for medical malpractice and conducting a feasibility study of a captive insurance company. There can be no assurance the Company will be able to obtain medical malpractice insurance on terms consistent with our current coverage, which may increase our cost.

Healthcare Regulatory Environment and Reliance on Government Programs -- The healthcare industry in general, and the services that the Company provides, are subject to extensive federal and state laws and regulations. Additionally, a significant portion of the Company's net revenue is from payments by government-sponsored health care programs, principally Medicare and Medicaid, and is subject to audit and adjustments by applicable regulatory agencies. Failure to comply with any of these laws or regulations, the results of increased regulatory audits and adjustments, or changes in the interpretation of the coding of services or the amounts payable for the Company's services under these programs could have a material adverse effect on the Company's financial position and results of operations. The Company's operations are continuously subject to review and inspection by regulatory authorities.

In August 2001, we received two letters from the United States Attorney for the Southern District of Ohio (the "U.S. Attorney") requesting information regarding billing practices and documentation of gross descriptions on skin biopsy reports. We provided documentation to the U.S. Attorney regarding the tests that were the subject of its requests for information. Requests for information such as these are often the

result of a qui tam, or whistleblower, action filed by a private party. In February 2002, we received notification that the U.S. Attorney would not pursue this matter any further. In addition, we were notified that there were then no presently pending lawsuits in the Southern District of Ohio against the Company relating to the request by any private party relator bringing a qui tam action.

Employment Agreements - The Company has entered into employment agreements with certain of its management employees, which include, among other terms, non-compete provisions and salary continuation benefits.

NOTE 7 - EARNINGS PER SHARE

Earnings per share is computed and presented in accordance with Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings Per Share." Basic earnings per share, which excludes the effects of any dilutive common equivalent shares that may be outstanding, such as shares issuable upon the exercise of stock options and warrants, is computed by dividing income attributable to common stockholders by the weighted average number of common shares outstanding for the respective periods. Diluted earnings per share gives effect to the potential dilution that could occur upon the exercise of certain stock options and warrants that were outstanding at various times during the respective periods presented. The dilutive effects of stock options and warrants are calculated using the treasury stock method.

Basic and diluted earnings per share for the respective periods are set forth in the table below (amounts in thousands, except per share amounts):

	Three Months Ended March 31
	2002

Earnings Per Common Share:		
Net income	$ 12,648	$
Basic earnings per common share	$ 0.42	$
Diluted earnings per common share	$ 0.41	$
Basic weighted average shares outstanding	30,325	
Effect of dilutive stock options and warrants	903	
Diluted weighted average shares outstanding	31,228	

Options to purchase 223,859 shares and 84,629 shares of common stock which were outstanding at March 31, 2002 and 2001, respectively, have been excluded from the calculation of diluted earnings per share for the respective years because their effect would be anti-dilutive.

AMERIPATH, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -
(Continued)

NOTE 8 - COMPREHENSIVE INCOME

The Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS 130"), which requires the Company to report and display certain information related to comprehensive income. As of December 31, 2001 and March 31, 2002 net income equaled comprehensive income.

NOTE 9 - SEGMENT REPORTING

The Company has two reportable segments, Owned and Managed practices. The segments were determined based on the type of service and customer. Owned practices provide anatomic pathology services to hospitals and referring physicians, while under the management relationships the Company provides management services to the affiliated physician groups. The accounting policies of the segments are the same as those described in the summary of accounting policies. The Company evaluates performance based on revenue and income before amortization of intangibles, merger-related charges, interest expense, other income and expense and income taxes ("Segment Operating Income"). In addition to the business segments above, the Company evaluates certain corporate expenses which are not allocated to the business segments.

The following is a summary of the financial information for the three months ended March 31 for the business segments and corporate.

Owned	2002	
Net patient service revenue	$105,802	$9
Operating income	31,319	2
Segment assets	414,198	27

Managed

Net management service revenue	$7,090	$
Operating income	781	
Segment assets	22,678	2
Corporate		
Operating loss	$(7,271)	$(
Segment assets	224,078	31
Elimination of intercompany accounts	(30,074)	(2

NOTE 10 - SUBSEQUENT EVENTS

Subsequent to March 31, 2002, the Company paid approximately $5.3 million relating to contingent notes issued in connection with previous acquisitions, which has been recorded as additional purchase price and an increase in goodwill.

In April 2002, the Company acquired Empire Pathology, a full service anatomic pathology located in Irvine, California.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

We are one of the leading national providers of anatomic pathology services. The more than 400 pathologists in our owned and managed operations as of March 31, 2002 provide medical diagnostic services in outpatient laboratories owned, operated and managed by us, in hospitals, and in ambulatory surgery centers. Under our ownership or employment model, we acquire a controlling equity (i.e., voting) interest or have a controlling financial interest in pathology operations. We refer to these operations as our owned operations. Under our management or equity model, we acquire certain assets of, and operate pathology laboratories under long-term management services agreements. We refer to these as our managed operations. Under the management services agreements, we provide facilities and equipment as well as administrative and technical support for the managed operations. As of March 31, 2002, we had six managed operations. When we refer to "companies" generally, we mean our owned and managed operations as a group.

As of March 31, 2002, our companies had contracts or business relationships with more than 200 hospitals pursuant to which we manage their clinical pathology and other laboratories and provide professional pathology services. The majority of these hospital contracts and relationships are exclusive provider relationships. We also have more than 40 licensed outpatient laboratories.

Generally, we manage and control all of the non-medical functions of the companies, including:

- recruiting, training, employing and managing the technical and support staff;
- developing, equipping and staffing laboratory facilities;
- establishing and maintaining courier services to transport specimens;
- negotiating and maintaining contracts with hospitals, national clinical

laboratories and managed care organizations and other payors;

- providing financial reporting and administration, clerical, purchasing, payroll, billing and collection, information systems, sales and marketing, risk management, employee benefits, legal, tax and accounting services;

- maintaining compliance with applicable laws, rules and regulations; and

- with respect to our ownership and operation of outpatient anatomic pathology laboratories, providing slide preparation and other technical services.

ACQUISITIONS

Since the first quarter of 1996, we have completed the acquisition of 50 pathology organizations located in 21 states. These acquisitions included the acquisition of Inform DX, during the fourth quarter of 2000. As a result of the Inform DX acquisition, we now have managed operations from which we derive management fees. Prior to the Inform DX transaction, we only had owned operations.

During the first three months of 2002, we acquired an operation located in Denver, CO which was previously managed by us under a management service agreement. The total consideration paid by us in connection with this acquisition included cash, consideration in the form of contingent notes and the assumption of certain liabilities. In addition, during the first quarter of 2002, we made contingent note payments of $17.7 million relating to previous acquisitions.

In April 2002, the Company acquired Empire Pathology, a full service anatomic pathology laboratory located in Irvine, California.

BUSINESS COLLABORATIONS

We have commenced our transition to becoming a fully integrated health care diagnostic information provider. As part of this transition, we have entered into business collaborations intended to generate additional revenues through leveraging our personnel, technology and resources. Three examples of such endeavors, including one with Genomics Collaborative, Inc. ("GCI"), one with Molecular Diagnostics, Inc. ("Molecular Diagnostics" (f/k/a Ampersand Medical of Chicago)), and one with TriPath Oncology, Inc. ("TriPath Oncology"), are described below. Although we believe such new endeavors are promising, we cannot assure you that they will be profitable.

During the third quarter of 2000, we formed an alliance with GCI to provide fresh frozen samples from normal, diseased, and cancerous tissue to GCI for subsequent sale to researchers in industry and academic laboratories who are working to discover genes associated with more common disease categories, such as heart disease, hypertension, diabetes, osteoporosis, depression, dementia, asthma and cancer, with a special focus on breast, colon and prostate tumors. This alliance utilizes our national network of hospitals, physicians and pathologists and GCI's capabilities in large-scale DNA tissue analysis and handling, tied together by proprietary information systems and bioinformatics. In connection with our alliance, we made a $1.0 million investment in GCI in exchange for 333,333 shares of Series D Preferred Stock, par value $0.01. The net revenue resulting from our alliance with GCI was not material to our operations during 2000 or 2001. Working with GCI, we have developed procedures to comply with informed consent requirements and other regulations regarding the

taking and processing of specimens from donors and related records. Failure to comply with such regulations could result in adverse consequences including potential liability to us.

On March 27, 2001, we announced an agreement with Molecular Diagnostics which illustrates another example of leveraging our existing resources. In this alliance, we will be performing clinical trial work for Molecular Diagnostics' cytology platform that utilizes proteomic biomarkers to help pathologists and cytologists identify abnormal and cancerous cells in pap smears and other body fluids, such as sputum and urine. We will be paid on a fee-for-service basis for each clinical trial we conduct. The agreement also calls for us to assist Molecular Diagnostics with the development of associated products and tests. We would receive equity in Molecular Diagnostics for the developmental work and would be entitled to royalty payments based on future sales of these products and tests. One of the Molecular Diagnostics products we are currently evaluating is a new test for human papilloma virus or HPV, which causes over 99% of all cervical dysplasia and cancer. This new test involves the application of genomic and proteomic markers directed against the specific oncogenes and oncoproteins of HPV that are directly responsible for the virus' ability to cause cancer. Preliminary studies indicate superior performance of these markers compared to currently available tests. However, there can be no assurance that such tests or such markers will be successful or become commercially viable.

On February 5, 2002, AmeriPath signed a letter of intent with TriPath Oncology to validate and offer exclusively a novel gene expression assay for Melastatin, a prognostic marker for melanoma. Melanoma represents the deadliest skin cancer whose incidence is rapidly increasing. Given our outstanding team of dermatopathologists and our market leadership in this field, we believe that this agreement may provide revenue to the Company as well as lead to additional opportunities.

SOURCES OF NET REVENUE

We derive our net revenue primarily from our owned and managed operations. Net revenue was comprised of net patient service revenue from our owned operations and net management service revenue from our managed operations.

The percent of our net revenue from outpatient and inpatient pathology and management services is presented below. The type and mix of business among these three categories, which can change from period to period as a result of new acquisitions and other factors, may change our ratio of operating costs to net revenue, particularly the provision for doubtful accounts as discussed below in our results of operations.

	Three Months Ended March 31,	
	2002	2001
Revenue Type		
Outpatient	48%	42%
Inpatient	46%	51%
Management service revenues	6%	7%

NET PATIENT REVENUES

The majority of services furnished by our pathologists are anatomic pathology diagnostic services. We typically bill government programs, principally Medicare and Medicaid, indemnity insurance companies, managed care organizations, national clinical laboratories, physicians and patients. Net patient revenue differs from amounts billed for services due to:

- Medicare and Medicaid reimbursements at annually established rates;
- payments from managed care organizations at discounted fee-for-service rates;
- negotiated reimbursement rates with national clinical laboratories and other third-party payors; and
- other discounts and allowances.

In many instances, the national clinical laboratories contract directly under capitated agreements with managed care organizations to provide clinical as well as anatomic pathology services. We, in turn, subcontract with national clinical laboratories to provide anatomic pathology services at a discounted fee-for-service rate and are, in most cases, attempting to increase the number of such subcontracts to increase test volume. Since the majority of our operating costs -- principally the compensation of physicians and non-physician technical personnel -- are relatively fixed, increases in test volume generally enhance our profitability. Historically, net patient service revenue from capitated contracts has represented an insignificant amount of total net patient service revenue. However, we may be required to enter into more capitated arrangements in order to compete effectively for managed care contracts in the future.

Virtually all of our net patient service revenue is derived from charging for services on a fee-for-service basis. Accordingly, we assume the financial risk related to collection, including potential uncollectability of accounts, long collection cycles for accounts receivable and delays in reimbursement by third-party payors, such as governmental programs, private insurance plans and managed care organizations. Increases in write-offs of doubtful accounts, delays in receiving payments or potential retroactive adjustments and penalties resulting from audits by payors may require us to borrow funds to meet current obligations or may otherwise have a material adverse effect on our financial condition and results of operations.

In addition to services billed on a fee-for-service basis, the hospital-based pathologists have supervision and oversight responsibility for their roles as Medical Directors of the hospitals' clinical, microbiology and blood banking operations. For this role, we bill non-Medicare patients according to a fee schedule for what is referred to as clinical professional component charges. For Medicare patients, the pathologist is typically paid a director's fee or a "Part A" fee by the hospital. Hospitals and third-party payors are continuing to

increase pressure to reduce the payment of these clinical professional component charges and "Part A" fees, and in the future we may sustain substantial decreases in these payments.

Approximately 23% of our collections in the first quarter of 2002 was from government-sponsored health care programs, principally Medicare and Medicaid, and is subject to audit and adjustments by applicable regulatory agencies. Failure to comply with any of these laws or regulations, the results of increased regulatory audits and adjustments, or changes in the interpretation of the coding of services or the amounts payable for services under these programs

could have a material adverse effect on our financial position and results of operations.

The impact of legislative changes on our results of operations will depend upon several factors, including the mix of inpatient and outpatient pathology services, the amount of Medicare business, and changes in reimbursement levels which are published in November of each year. Management continuously monitors changes in legislation impacting reimbursement.

In prior years, we have been able to mitigate the impact of reductions in Medicare reimbursement rates for anatomic pathology services through the achievement of economies of scale and production efficiencies. Despite any offsets, the recent substantial modifications to the physician fee schedule, along with additional adjustments by Medicare, could have a material adverse effect on average unit reimbursement in the future. In addition, other third-party payors could adjust their reimbursement based on changes to the Medicare fee schedule. Any reductions made by other payors could also have a material negative impact on average unit reimbursement.

NET MANAGEMENT SERVICE REVENUE

Net management service revenue is based on a predetermined percentage of operating income of the managed operations, before physician group retainage, plus reimbursement of certain practice expenses as defined in each management service agreement. Management fees are recognized at the time the net physician group revenue is recorded by the physician group.

Generally, net management service revenue equates to net physician group revenue less amounts retained by the physician groups, which we refer to as physician group retainage. Net physician group revenue is equal to billed charges reduced by provisions for bad debt and contractual adjustments. Contractual adjustments represent the difference between amounts billed and amounts reimbursable by commercial insurers and other third-party payors pursuant to their respective contracts with the physician group. The provision for bad debts represents an estimate of potential credit issues associated with amounts due from patients, commercial insurers, and other third-party payors. Net physician group revenue, which underlies our management service revenue, is subject to the same legislative and regulatory factors discussed above with respect to net patient revenue.

MEDICARE REIMBURSEMENT

Since 1992 the Centers for Medicare and Medicaid Services ("CMS") (formerly known as the Health Care Financing Administration, or "HCFA") had paid for physician's services under section 1848 of the Social Security Act. CMS calculates and reimburses fees for all physician services ("Part B" fees), including anatomic pathology services, based on a fee schedule methodology known as the resource-based relative value system ("RBRVS"). The RBRVS initially was phased in over a four-year period. Subsequently, CMS proposed changes in the computation of the malpractice portion and practice expense portion of the relative value units ("RVUs"). Although these changes have changed reimbursement to some extent, they are not expected to have a material impact on the Company's revenues. Overall, anatomic pathology reimbursement rates declined during the fee schedule phase-in period, despite an increase in payment rates for certain pathology services performed by us.

The Medicare Part B fee schedule payment for each service is determined by multiplying the total RVUs established for the service by a Geographic Practice Cost Index ("GPCI"). The sum of this value is

multiplied by a statutory conversion factor. The number of RVUs assigned to each service is in turn calculated by adding three separate components: work RVU (intensity of work), practice exposure RVU (expense related to performing the service) and malpractice RVU (malpractice costs associated with the service).

CMS reviews annually the RBRVS payment schedule in conjunction with its budgeting process. The resulting payment schedule is published each year in the Federal Register in November. The blended payment rates for services provided by AmeriPath to Medicare patients, based on our values and locations of services, increased by 11.3% from 1999 to 2000, and by 6.8% from 2000 to 2001. However, there can be no assurance that we will receive similar increases in the future, and it is possible that our blended rates may decrease at some point in the future.

A final rule published in the Federal Register on November 1, 2001 indicates that the conversion factor used in the Medicare Physician Fee Schedule was reduced by 5.4%. The RVUs were also changed in 2002, with certain services getting an increase in RVUs, while others are decreased. We estimate the overall impact to be neutral for 2002.

In 1999, CMS announced that it would cease the direct payment by Medicare for the technical component of inpatient physician pathology services to an outside independent laboratory because they concluded payment for the technical component is included already in the payment to hospitals under the hospital inpatient prospective payment system. Implementation of this change commenced January 1, 2001. Under these rules, independent pathology laboratories would be required to bill the hospital directly for technical services on hospital Medicare inpatients. Congress, however, "grandfathered," for a period of two years, certain existing hospital-lab arrangements in effect before July 22, 1999. Effective January 2001, hospital arrangements that were not grandfathered are not reimbursed by Medicare for the technical component. The majority of our hospital arrangements were grandfathered under the proposed rules. Upon expiration of the two years, the grandfather provision is scheduled to expire.

Additionally, with the implementation of the hospital outpatient prospective payment system ("PPS") during 2000, independent pathology laboratories providing technical services to Medicare hospital outpatients generally are no longer able to bill Medicare for the technical component ("TC") of those services. Rather, they need to bill the hospital for the TC. The hospital is reimbursed as part of the new Ambulatory Payment Classification ("APC") payment system. Laboratories providing these services now need to contract directly with hospitals for reimbursement. As the amount paid to hospitals for the most common pathology services is less than the technical component under the RBRVS, it is likely that those laboratories will incur substantial reductions in reimbursement under PPS. However, services provided by us which are subject to PPS are not material to our total net revenue.

MANAGED CARE CONTRACTING

The Company signed two new managed care agreements in the first quarter of 2002. First, the Company announced the signing of a nationwide PPO agreement covering 15 million Aetna/U.S. Healthcare members, as well as a statewide HMO, capitated agreement in Florida for 750,000 HMO lives. Secondly, we signed a fee-for-service agreement with Independence Blue Cross/Keystone in Philadelphia covering one million lives. The contract, which is critical to our market growth, was the result of market demand to Keystone for AmeriPath's quality local diagnostic services.

In addition, during the quarter we signed new contracts with 12 other payors, generally on a non-exclusive fee-for-service basis, covering approximately 3.4 million lives.

CRITICAL ACCOUNTING POLICIES AND METHODS

Intangible Assets

As of March 31, 2002, we had net identifiable intangible assets and goodwill of $257.1 million and $237.6 million, respectively. Management assesses on an ongoing basis if there has been an impairment in the carrying value of its intangible assets. If the undiscounted future cash flows over the remaining amortization period of the respective intangible asset indicates that the value assigned to the intangible asset may not be recoverable, the carrying value of the respective intangible asset will be reduced. The amount of any such impairment would be determined by comparing anticipated discounted future cash flows from acquired businesses with the carrying value of the related assets. In performing this analysis, management considers such factors as current results, trends and future prospects, in addition to other relevant factors. Significant changes in our future cash flow resulting from events such as loss of hospital or national lab contracts, physician referrals, or management service agreements could result in further charge offs of intangible assets.

Identifiable intangible assets include hospital contracts, physician referral lists, laboratory contracts, and management service contracts acquired in connection with acquisitions. Such assets are recorded at fair value the date of acquisition as determined by management and are being amortized over the estimated periods to be benefited, ranging from 10 to 40 years. In determining these lives, the Company considered each practice's operating history, contract renewals, stability of physician referral lists and industry statistics. If circumstances change, indicating a shorter estimated period of benefit, future amortization expense could increase.

Revenue Recognition

The Company recognizes net patient service revenue at the time services are performed. Unbilled receivables are recorded for services rendered during, but billed subsequent to, the reporting period. Net patient service revenue is reported at the estimated realizable amounts from patients, third-party payors and others for services rendered. Revenue under certain third-party payor agreements is subject to audit and retroactive adjustments. Provision for estimated third-party payor settlements and adjustments are estimated in the period the related services are rendered and adjusted in future periods as final settlements are determined. The provision and the related allowance are adjusted periodically, based upon an evaluation of historical collection experience with specific payors for particular services, anticipated collection levels with specific payors for new services, industry reimbursement trends, and other relevant factors. Changes in these factors in future periods could result in increases or decreases in the provision, our results of operations and financial position.

Contingent Purchase Price

Our acquisitions, except for the pooling with Inform DX, have been accounted for using the purchase method of accounting. The aggregate consideration paid, and to be paid, is based on a number of factors, including the acquired operation's demographics, size, local prominence, position in the marketplace and historical cash flows from operations. Assessment of these and other factors, including uncertainties regarding the health care environment, resulted in the sellers and the Company being unable to reach agreement on the final purchase price. We agreed to pay a minimum purchase price and to pay additional purchase price considerations to the sellers in proportion to their respective ownership

interest. The additional payments are contingent upon the achievement of stipulated levels of operating earnings (as defined) by each of the operations over periods of three to five years from the date of the acquisition as set forth in the respective agreements, and are not contingent on the continued employment of the sellers. In certain cases, the payments are contingent upon other factors such as the retention of certain hospital contracts for periods ranging from three to five years. The amount of the payments cannot be determined until the achievement of the operating earnings levels or other factors during the terms of the respective agreements. Additional payments made in connection with the contingent notes are accounted for as additional purchase price, which increases the recorded goodwill and, in

accordance with accounting principles, generally accepted in the United States of America, are not reflected in our results of operations.

Provision for Doubtful Accounts

The provision for doubtful accounts is estimated in the period the related services are rendered and adjusted in future accounting periods as necessary. The estimates for the provision and the related allowance are based on an evaluation of historical collection experience, the aging profile of the accounts receivable, the historical doubtful account write-off percentages, revenue channel (i.e., inpatient vs. outpatient) and other relevant factors. Changes in these factors in future periods could result in increases or decreases in the provision, our results of operations and financial position.

Principles of Consolidation

Our consolidated financial statements include the accounts of AmeriPath, Inc., its wholly-owned subsidiaries, and companies in which the Company has the controlling financial interest by means other than the direct record ownership of voting stock. Intercompany accounts and transactions have been eliminated. If it was determined that we do not have a controlling financial interest for any or all companies where we do not have a direct ownership of voting stock, the results of operations could be materially affected. We do not consolidate the affiliated physician groups we manage as we do not have controlling financial interest as described in EITF 97-2.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2002 AND 2001

Changes in the results of operations between the three month periods ended March 31, 2002 and 2001 are due primarily to the various acquisitions which were consummated by the Company subsequent to March 31, 2001. Reference to same store means practices at which we provided services for the entire period for which the amount is calculated and the entire prior comparable period, including de novo (start-up) operations and expanded ancillary testing services added to existing operations. During the first three months of 2002, the Company completed one acquisition.

PERCENTAGE OF NET REVENUE

The following table sets forth, for the periods indicated, certain consolidated financial data as a percentage of net revenue (billings net of contractual and other allowances):

	Three Months E March 31,
	2002
NET REVENUES	100.0%
OPERATING COSTS AND EXPENSES:	
Cost of services	48.1%
Selling, general and administrative expenses	17.8%
Provision for doubtful accounts	12.1%
Amortization expense	2.5%
Merger-related charges	--
Total operating costs and expenses	80.5%
INCOME FROM OPERATIONS	19.5%
Interest expense and other, net	.8%
INCOME BEFORE INCOME TAXES	18.7%
PROVISION FOR INCOME TAXES	7.5%
NET INCOME	11.2%

Net Revenues

Net revenues increased by $14.2 million, or 14.4%, from $98.7 million for the three months ended March 31, 2001, to $112.9 million for the three months ended March 31, 2002. Same store net revenue increased $11.6 million or 11.7% from $98.7 million for the three months ended March 31, 2001 to $110.3 million for the three months ended March 31, 2002. We estimate that 3% of the same store revenue increase was attributable to price and the remaining 9% of the same store revenue increase was attributable to volume and mix. Same store outpatient revenue increased $7.3 million, or 16.5%, same store hospital revenue increased $3.3 million, or 6.9%, and same store management service revenue increased $1.0 million, or 14.7%, compared to the same period of the prior year. The remaining increase in revenue of $2.6 million resulted from acquired operations. Our mix of revenue for the first quarter of 2002 was 48% outpatient, 46% inpatient (hospital based) and 6% management services.

During the three months ended March 31, 2002, approximately $6.8 million, or 6.0%, of the Company's net revenue was attributable to contracts with national labs including Quest Diagnostics ("Quest") and Laboratory Corporation of America Holdings ("LabCorp"). We are currently experiencing substantial declines in volume from Quest work in our Philadelphia laboratory. As a result, we are attempting to broaden our customer base in this market to lessen any potential impact. There can be no assurances that we will be able to recover lost volume. Our decision or decisions by Quest or LabCorp to discontinue processing work from the national laboratories, could materially harm our financial position and results of operations, including the potential impairment of intangible assets. As of March 31, 2002, we had net identifiable intangible assets related to lab

contracts of $2.8 million.

In addition, approximately $12.1 million, or 10.8%, of the Company's net revenue is derived from 29 hospitals operated by HCA, Inc. ("HCA"), formerly known as Columbia/HCA Healthcare Corporation. Generally, any contracts or relationships we may have with these and other hospitals are short-term and allow for termination by either party with relatively short notice. HCA has been under government investigation for some time, and we believe that HCA is evaluating its operating strategies, including the possible sale, spin-off or closure of certain hospitals. Closures or sales of HCA hospitals or terminations or non-renewals of one or more of our contracts or relationships with HCA hospitals could have a material adverse effect on our financial position and results of operations.

Cost of Services

Cost of services consists principally of the compensation and fringe benefits of pathologists, licensed technicians and support personnel, laboratory supplies, shipping and distribution costs and facility costs.

Cost of services increased by $5.9 million, or 12.2%, from $48.4 million for the three months ended March 31, 2001 to $54.3 million for the same period in 2002. Cost of services, as a percentage of net revenues, decreased from 49.0% for the three months ended March 31, 2001 to 48.1% in the comparable period of 2002. Gross margin increased from 51.0% in the three months ended March 31, 2001 to 51.9% in 2002. The increase over the prior year was due in part to synergies from the Inform DX acquisition with some offset by higher costs.

Selling, General and Administrative Expenses

The cost of corporate support, sales and marketing, and billing and collections comprise the majority of what is classified as selling, general and administrative expenses ("SG&A"). As a percentage of consolidated net revenues, SG&A increased from 17.4% for the three months ended March 31, 2001 to 17.8% for the same period of 2002, as the Company continues to invest in marketing, information systems and billing operations.

SG&A increased by $2.8 million, or 16.3%, from $17.2 million for the three months ended March 31, 2001 to $20.0 million for the comparable period of 2002. Of this increase, approximately $800,000 was attributable to the increase in billing and collection costs which typically increases as revenue and cash collections increase. In addition, in connection with our focus on increasing our sales and marketing and information technology efforts, these costs increased $1.2 million and $443,000, respectively. The increase in marketing costs includes the cost of additional marketing personnel to cover new markets for dermatopathology, marketing literature, and products to expand our penetration in the urology, gastroenterology and oncology markets. The remaining increase was due primarily to increased staffing levels in human resources and accounting, salary increases, and costs incurred to expand our administrative support infrastructure and to enhance our services.

Provision for Doubtful Accounts

The provision for doubtful accounts increased by $3.0 million, or 28.0%, from $10.7 million for the three months ended March 31, 2001, to $13.7 million for the same period in 2002. The provision for doubtful accounts as a percentage of net revenues was 10.8% and 12.1% for the three month periods ended March 31, 2001 and 2002, respectively. This increase was related primarily to a change in revenue mix. The mix change relates, in part, to the shift from Quest and

management service revenues, which carry zero bad debt, to outpatient and hospital revenues. In addition, within the hospital mix, there was an increase in clinical professional component billing which carries a higher bad debt percentage.

Amortization Expense

Amortization expense decreased by $1.7 million, or 37.8%, from $4.5 million for the three months ended March 31, 2001, to $2.8 million for the same period of 2002. The decrease is attributable to the

discontinuance of goodwill amortization as promulgated by Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets", which was effective January 1, 2002. Identifiable intangible amortization expense is expected to increase in the future as a result of additional identifiable intangible assets arising from future acquisitions.

We continually evaluate whether events or circumstances have occurred that may warrant revisions to the carrying values of our goodwill and other identifiable intangible assets, or to the estimated useful lives assigned to such assets. Any significant impairment recorded on the carrying values of our goodwill or other identifiable intangible assets could materially harm results of operations. Such impairment would be recorded as a charge to operating profit and reduction in intangible assets.

Merger-related Charges

The merger-related charges of $7.1 million for the three months ended March 31, 2001 relate to AmeriPath's acquisition of Inform DX and include transaction costs and costs related to the closing of the Inform DX corporate office in Nashville and the consolidation or closing of the overlapping operations of Inform DX in New York and Pennsylvania. The restructuring of the combined operations of AmeriPath and Inform DX resulted in annual operating synergies of approximately $5 million.

Income from Operations and Net Income

Income from operations increased $11.2 million, or 103.7%, from $10.8 million for the three months ended March 31, 2001, to $22.0 million in the same period of 2002. Without the merger-related charges, income from operations would have increased by $4.1 million, or 23.1%.

Net income for the three months ended March 31, 2002 was $12.6 million, an increase of $9.4 million, or 293.8%, over the same period in 2001. Diluted earnings per share for the three months ended March 31, 2002 increased to $0.41 from $0.12 for the comparable period of 2001, based on 31.2 million and 26.0 million weighted average shares outstanding, respectively. Diluted earnings per share would have been $0.30 without the merger-related charge in the first quarter of 2001.

Interest Expense

Interest expense decreased by $3.6 million, or 76.6%, from $4.7 million for the three months ended March 31, 2001, to $1.1 million for the same period in 2002. This decrease was attributable to a combination of lower average amount of debt outstanding and lower interest rates during the three months ended March 31, 2002. For the three months ended March 31, 2002, average indebtedness outstanding was $99.3 million, compared to average indebtedness of $207.3 million outstanding in the same period of 2001. The Company's effective interest

rate was 4.2% and 9.2% for the three month periods ended March 31, 2002 and 2001, respectively. The decrease in the average indebtedness was due to the Company completing a secondary offering and using the proceeds to repay debt in the fourth quarter of 2001. In addition, during the fourth quarter of 2001, the Company entered into a new credit facility agreement. The new credit facility has a borrowing rate based on the Company's leverage ratio. As of March 31, 2002, the borrowing rate was LIBOR plus 150 basis points.

Provision for Income Taxes

The effective income tax rate was approximately 46.8% and 40.0% for the three month period ended March 31, 2001 and 2002, respectively. In the quarter ended March 31, 2001, the effective tax rate is higher than AmeriPath's statutory rates primarily due to the non-deductibility of the goodwill amortization related to the Company's acquisitions. In addition, for the three-month period ended March 31, 2001, the Company had non-deductible merger-related charges, which further increased the effective tax rate. The effective tax rate for the three-month period ended March 31, 2001, excluding these items and goodwill would have been approximately 40.3%.

LIQUIDITY AND CAPITAL RESOURCES

At March 31, 2002, the Company had working capital of approximately $56.9 million, an increase of $0.1 million from the working capital of $56.8 million at December 31, 2001. The increase in working capital was due primarily to the increase in net accounts receivable of $4.3 million and other assets of $0.7 million offset by a reduction in cash and cash equivalents of $3.8 million and an increase in accounts payable and accrued expenses of $1.1 million.

For the three month periods ended March 31, 2001 and 2002, cash flows from operations were $11.7 million and 11.9% of net revenue, and $13.5 million and 12.0% of net revenue, respectively. Excluding pooling merger-related charges incurred by Inform DX and paid by us of $1.5 million in the first quarter of 2001, cash flow from operations would have been $13.2 million. For the three months ended March 31, 2002, cash flow from operations and borrowings under the Company's credit facility were used to make contingent note payments of $17.7 million, fund an acquisition of $6.9 million, and acquire $1.7 million of property and equipment.

At March 31, 2002, the Company had $103.0 million available under its credit facility with a syndicate of banks. The credit facility provides for borrowings of up to $200 million, with commitments totaling $175 million, in the form of a revolving loan that may be used for working capital purposes and to fund acquisitions. As of March 31, 2002, $97.0 million was outstanding under the revolving loan with an annual effective interest rate of 4.24%.

The credit facility has a five-year term with a final maturity date of November 30, 2006. Interest is payable monthly at variable rates which are based, at the Company's option, on the agent's base rate (4.75% at March 31, 2002) or the LIBOR rate plus a premium that is based on the Company's ratio of total funded debt to pro forma consolidated earnings before interest, taxes, depreciation and amortization. As of March 31, 2002, the LIBOR premium was 1.5%. The new facility also requires a commitment fee to be paid quarterly equal to 0.375% of the unused portion of the total commitment. The credit facility has three basic financial covenants regarding leverage, fixed charge coverage and interest coverage. In addition, the agreement has a number of nonfinancial covenants. At March 31, 2002, we are in compliance with the covenants of the credit facility. The unused commitments under the credit facility will be used for general working capital needs and our acquisition program.

During the first quarter of 2002, the Company acquired an operation which was previously managed under a management services agreement. Total consideration paid consisted of cash, consideration in the form of contingent notes and the assumption of certain liabilities.

In connection with all of our acquisitions, we generally agree to pay a base purchase price plus additional contingent purchase price consideration to the sellers of the practices. The additional payments are generally contingent upon the achievement of stipulated levels of operating earnings by the acquired practices over periods of three to seven years (generally five years) from the date of the acquisition, and are

not contingent on the continued employment of the sellers of the practices. In certain cases, the payments are contingent upon other factors such as the retention of certain hospital contracts or relationships for periods ranging from three to five years. The amount of the payments cannot be determined until the achievement of the operating earnings levels or other factors during the terms of the respective agreements. If the maximum specified levels of operating earnings for each acquired practice are achieved, we would make aggregate maximum payments, including principal and interest, of approximately $140.9 million over the next three to five years. A lesser amount or no payments at all would be made if the stipulated levels of operating earnings specified in each agreement were not met. In the first quarter of 2002, we made contingent note payments aggregating $17.7 million. These contingent note payments are currently estimated to be $18-$19 million and $34-35 million for the remainder of 2002 and the year 2003, respectively. After 2003 these payments are projected to decline.

We expect to continue to use our credit facility to fund acquisitions and for working capital. We anticipate that funds generated by operations and funds available under our credit facility will be sufficient to meet working capital requirements and anticipated contingent note obligations, and to finance capital expenditures over the next 12 months. Further, in the event additional payments under the contingent notes issued in connection with acquisitions become due, we believe that the incremental cash generated from operations would exceed the cash required to satisfy our payment, if any, of the contingent obligations in any one-year period. Such payments, if any, will result in a corresponding increase in goodwill. Funds generated from operations and funds available under the credit facility may not be sufficient to implement our longer-term growth strategy. We may be required to seek additional financing through additional increases in the credit facility, to negotiate credit facilities with other banks or institutions or to seek additional capital through private placements or public offerings of equity or debt securities. No assurances can be given that we will be able to extend or increase the existing credit facility, secure additional bank borrowings or complete additional debt or equity financings on terms favorable to us or at all.

QUALIFICATION OF FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Statements contained anywhere in this Form 10-Q that are not limited to historical information are considered forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including, without limitation, statements regarding the Company's expectations, beliefs, intentions, plans or

strategies regarding the future. These forward-looking statements are based largely on the Company's expectations which are subject to a number of known and unknown risks, uncertainties and other factors discussed in this report and in other documents filed by the Company with the Securities and Exchange Commission (including, without limitation, the Company's Annual Report on Form 10-K for the year ended December 31, 2001), which may cause actual results to be materially different from those anticipated, expressed or implied by the forward-looking statements. All forward-looking statements included in this document are based on information available to the Company on the date hereof, and the Company assumes no obligation to update any such forward-looking statements to reflect future events or circumstances. Forward-looking statements are sometimes indicated by words such as "may," "should," "believe," "expect," "anticipate" and similar expressions.

In addition to the risks and uncertainties identified elsewhere herein and in other documents filed by the Company with the Securities and Exchange Commission, the following factors should be carefully considered when evaluating the Company's business and future prospects: general economic conditions; competition and changes in competitive factors; the extent of success of the Company's operating initiatives and growth strategies (including without limitation, the Company's continuing efforts to (i) achieve continuing improvements in performance of its current operations, by reason of various synergies, marketing efforts, revenue growth, cost savings or otherwise, (ii) transition into becoming a fully integrated healthcare diagnostic information provider, including the Company's efforts to develop, and the Company's investment in, new products, services, technologies and related alliances, such as the alliance with Genomics Collaborative, Inc. (iii) acquire or develop additional pathology practices (as further described below), and (iv) develop and expand its managed care and national clinical lab contracts; federal and state

healthcare regulation (and compliance); reimbursement rates under government-sponsored and third party healthcare programs and the payments received under such programs; changes in coding; changes in technology; dependence upon pathologists and contracts; the ability to attract, motivate, and retain pathologists; labor and technology costs; marketing and promotional efforts; the availability of pathology practices in appropriate locations that the Company is able to acquire on suitable terms or develop; the successful completion and integration of acquisitions (and achievement of planned or expected synergies); access to sufficient amounts of capital on satisfactory terms; and tax laws. In addition, the Company's strategy to penetrate and develop new markets involves a number of risks and challenges and there can be no assurance that the healthcare regulations of the new states in which the Company enters and other factors will not have a material adverse effect on the Company. The factors which may influence the Company's success in each targeted market in connection with this strategy include: the selection of appropriate qualified practices; negotiation, execution and consummation of definitive acquisition, affiliation, management and/or employment agreements; the economic stability of each targeted market; compliance with state, local and federal healthcare and/or other laws and regulations in each targeted market (including health, safety, waste disposal and zoning laws); compliance with applicable licensing approval procedures; restrictions under labor and employment laws, especially non-competition covenants. Past performance is not necessarily indicative of future results. Certain risks, uncertainties and other factors discussed or noted above are more fully described elsewhere in this report, including under the caption - "Risk Factors" below.

RISK FACTORS

You should carefully consider each of the following risks and all of the other information set forth in this Form 10-Q. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial may also adversely affect our business.

If any of the following risks actually occur, our business prospects, financial condition and results of operations could be materially adversely affected and the trading price of our common stock could decline. In any such case, you could lose all or part of your investment in our company.

Our business could be materially harmed by future interpretation or implementation of state laws regarding prohibitions on the corporate practice of medicine.

We acquire or affiliate with pathology operations located in many states across the country. However, the laws of many states prohibit business corporations, including AmeriPath and its subsidiaries, from owning corporations that employ physicians, or from exercising control over the medical judgments or decisions of physicians. These laws and their interpretations vary from state to state and are enforced by both the courts and regulatory authorities, each with broad discretion. The manner in which we operate each organization is determined primarily by the corporate practice of medicine restrictions of the state in which the organization is located and other applicable regulations.

We believe that we are currently in material compliance with the corporate practice of medicine laws in each of the states in which we operate. Nevertheless, it is possible that regulatory authorities or other parties may assert that we are engaged in the unauthorized corporate practice of medicine. If such a claim were successfully asserted in any jurisdiction, we could be subject to civil and criminal penalties, which could exclude us from participating in Medicare, Medicaid and other governmental health care programs, or we could be required to restructure our contractual and other arrangements. Any restructuring of our contractual and other arrangements with our operations could result in lower revenues, increased expenses and reduced influence over the business decisions of those operations. Alternatively, some of our existing contracts could be found to be illegal and unenforceable, which could result in the termination of those contracts and an associated loss of revenue. In addition, expansion of our operations to other corporate practice states may require structural and organizational modification to the form of relationships that we currently have with our operations and hospitals. Such modifications could result in less profitable operations, less influence over the business decisions and failure to achieve our growth objectives.

We could be hurt by future interpretation or implementation of federal and state anti-kickback laws.

Federal anti-kickback laws and regulations prohibit the offer, payment, solicitation and receipt of any form of remuneration in exchange for referrals of products or services for which payment may be made by Medicare, Medicaid or other federal health care programs. Violations of federal anti-kickback laws are punishable by monetary fines, civil and criminal penalties and exclusion from participation in Medicare, Medicaid and other governmental health care programs. Several states have similar laws. While we believe our operations are in material compliance with applicable Medicare and fraud and abuse laws, including the anti-kickback law, there is a risk that government authorities might take a contrary position or might investigate our arrangements with physicians and third parties, particularly those arrangements that do not satisfy the compliance safe harbors provided under the relevant regulations or that are

similar to arrangements found to be problematic in advisory opinions of the Department of Health and Human Services Office of Inspector General (OIG). For example, the OIG has addressed physician practice management arrangements in an advisory opinion and found that management fees based on a percentage of practice revenues may violate the federal anti-kickback statute. While we believe our fee arrangements can be distinguished from those addressed in the opinion, government authorities may disagree. Such occurrences, regardless of their outcome, could damage our reputation and adversely affect important business relationships that we have with third parties, including physicians, hospitals and private payors. If our arrangements with physicians and third parties were found to be illegal, we could be subject to civil and criminal penalties, including fines and possible exclusion from participation in government payor programs. Significant fines could cause liquidity problems and adversely affect our results of operations. Exclusion from participation in government payor programs, which represented 23% of our collections from owned operations in the first quarter of 2002, would eliminate an important source of revenue and could materially adversely affect our business. In addition, some of our existing contracts could be found to be illegal and unenforceable, which could result in the termination of those contracts and an associated loss of revenue.

Our business could be harmed by future interpretation or implementation of the federal Stark Law and other state and federal anti-referral laws.

We are also subject to federal and state statutes and regulations banning payments for referrals of patients and referrals by physicians to health care providers with whom the physicians have a financial relationship. The federal Stark Law applies to Medicare and Medicaid and prohibits a physician from referring patients for certain services, including laboratory services, to an entity with which the physician has a financial relationship.

Financial relationship includes both investment interests in an entity and compensation arrangements with an entity. The state laws and regulations vary significantly from state to state, are often vague and, in many cases, have not been interpreted by courts or regulatory agencies. These state laws and regulations generally apply to services reimbursed by both governmental and private payors. Violations of these federal and state laws and regulations may result in prohibition of payment for services rendered, loss of licenses, fines, criminal penalties and exclusion from governmental and private payor programs. We have financial relationships with our pathologists, as defined by the federal Stark Law, in the form of compensation arrangements, ownership of our common stock and contingent promissory notes issued by us in connection with acquisitions. While we believe that our financial relationships with pathologists and referral practices are in material compliance with applicable laws and regulations, government authorities might take a contrary position or prohibited referrals may occur. We cannot be certain that pathologists who own our capital stock or hold contingent promissory notes will not violate these laws or that we will have knowledge of the identity of all beneficial owners of our capital stock. If our financial relationships with pathologists were found to be illegal, or if prohibited referrals were found to have been made, we could be subject to civil and criminal penalties, including fines, exclusion from participation in government and private payor programs and requirements to refund amounts previously received from government and private payors. In addition, expansion of our operations to new jurisdictions, or new interpretations of laws in our existing jurisdictions, could require structural and organizational modifications of our relationships with physicians to comply with that jurisdiction's laws. Such structural and organizational modifications could result in lower profitability and failure to achieve our growth objectives.

Our business could be materially harmed by future interpretation or implementation of state laws regarding prohibitions on fee-splitting.

Many states prohibit the splitting or sharing of fees between physicians and non-physicians. These laws vary from state to state and are enforced by courts and regulatory agencies, each with broad discretion. Some states have interpreted management agreements between entities and physicians as unlawful fee-splitting. We believe our arrangements with physicians comply in all material respects with the fee-splitting laws of the states in which we operate. Nevertheless, it is possible regulatory authorities or other parties could claim we are engaged in fee-splitting. If such a claim were successfully asserted in any jurisdiction, our pathologists could be subject to civil and criminal penalties and we could be required to restructure our contractual and other arrangements. Any restructuring of our contractual and other arrangements with our operations could result in lower revenues, increased expenses in the operations and reduced influence over the business decisions. Alternatively, some of our existing contracts could be found to be illegal and unenforceable, which could result in the termination of those contracts and an associated loss of revenue. In addition, expansion of our operations to other states with fee-splitting prohibitions may require structural and organizational modification to the form of our current relationships. Any modifications could result in less profitable relationships, less influence over the business decisions of and failure to achieve our growth objectives.

We could be hurt by future interpretation or implementation of state and federal anti-trust laws.

In connection with the corporate practice of medicine laws, the operations with which we are affiliated in some states are organized as separate legal entities. As such, the separate legal entities may be deemed to be persons separate both from us and from each other under the antitrust laws and, accordingly, subject to a wide range of laws that prohibit anti-competitive conduct among separate legal entities. In addition, we are seeking to acquire or affiliate with established and reputable pathology organizations in new geographic markets. While we believe that we are in material compliance with these laws and intend to comply with any laws that may apply to our development of integrated health care delivery networks, courts or regulatory authorities could nevertheless take a contrary position or investigate our business practices. If our business practices were found to violate these laws, we could be required to pay substantial fines, penalties and damage awards, or we could be required to restructure our business in a manner that would materially reduce our profitability or impede our growth.

Our business could be harmed by future interpretation or implementation of the Health Care Insurance Portability and Accountability Act.

The Health Care Insurance Portability and Accountability Act, or HIPAA, created provisions that impose criminal penalties for fraud against any health care benefit program, for theft or embezzlement involving health care and for false statements in connection with the payment of any health benefits. The HIPAA provisions apply not only to federal programs, but also to private health benefit programs. HIPAA also broadened the authority of the OIG to exclude participants from federal health care programs. Because of the uncertainties as to how the HIPAA provisions will be enforced, we are currently unable to predict their ultimate impact on us. Compliance with HIPAA could cause us to modify our business operations in a manner that would increase our operating costs or impede our growth. In addition, although we are unaware of any current violations of HIPAA, if we were found to be in violation of HIPAA, the

government could seek penalties against us or seek to exclude us from participation in government payor programs. Significant fines could cause liquidity problems and adversely affect our results of operations. Exclusion from participation in government payor programs, which represented 23% of collections for 2002, would eliminate an important source of revenue and could materially adversely affect our business.

Federal and state regulation of the privacy, security and transmission of health information could restrict our operations, impede the implementation of our business strategies or cause us to incur significant costs.

The privacy, security and transmission of health information is subject to federal and state laws and regulations, including HIPAA. Some of our operations will be subject to HIPAA and its regulations. Because HIPAA's privacy regulations do not supercede state laws that are more stringent, we will have to comply both with the federal privacy regulations under HIPAA and with any state privacy laws that are more stringent than HIPAA. Our operations that are subject to HIPAA must be in compliance with HIPAA's regulations by April 2003. Another set of regulations issued under HIPAA establishes uniform standards relating to data reporting, formatting, and coding that covered entities must use when conducting certain transactions involving health information. The compliance date for these regulations is October 2002. A third set of regulations, which have not yet been finalized, will establish minimum security requirements to protect health information. The HIPAA regulations could result in significant financial obligations for us and will pose increased regulatory risk. The privacy regulations could limit our use and disclosure of patient health information and could impede the implementation of some of our business strategies, such as our genomics initiatives. For example, the Department of Health and Human Services, or HHS, has indicated that cells and tissues are not protected health information, but that analyses of them are protected. HHS has stated that if a person provides cells to a researcher and tells the researcher that the cells are an identified individual's cancer cells, that accompanying statement is protected health information. At this time, we are unable to determine the full impact of the HIPAA regulations on our business and our business strategies or the total cost of complying with the regulations, but the impact and the cost could be significant. Many states have enacted, or indicated an intention to enact, privacy laws similar to HIPAA. These state laws could also restrict our operations, impede the implementation of our business strategies or cause us to incur significant compliance costs. In addition, failure to comply with federal or state privacy laws and regulations could subject us to civil or criminal penalties.

We charge our clients on a fee-for-service basis, so we incur financial risk related to collections as well as potentially long collection cycles when seeking reimbursement from third-party payors.

Substantially all of our net revenues are derived from our operations' charging for services on a fee-for-service basis. Accordingly, we assume the financial risk related to collection, including the potential uncollectability of accounts, long collection cycles for accounts receivable and delays attendant to reimbursement by third-party payors, such as governmental programs, private insurance plans and managed care organizations. Our provision for doubtful accounts for the quarter ended March 31, 2002 was 12.1% of net revenues, with net revenues from inpatient services having a provision for doubtful accounts of approximately 20.5%. If our revenue from hospital-based services increases as a percentage of our total net revenues, our provision for doubtful accounts as a percentage of total net revenues may increase. Increases in write-offs of doubtful accounts, delays in receiving payments or potential retroactive adjustments and penalties resulting from audits by payors may adversely affect our operating cash flow and liquidity, require us to borrow funds to meet our current obligations, reduce our profitability, impede our growth or otherwise materially adversely affect our business.

We rely upon reimbursement from government programs for a significant portion of our collections, and therefore our business would be harmed if reimbursement rates from government programs decline.

We derived 23% of our collections in the first quarter of 2002 from payments made by government sponsored health care programs, principally Medicare and Medicaid. These programs are subject to substantial regulation by federal and state governments. Any changes in reimbursement regulations, policies, practices, interpretations or statutes that place limitations on reimbursement amounts or change reimbursement coding practices could materially harm our business by reducing revenues and lowering profitability. Increasing budgetary pressures at both the federal and state levels and concerns over escalating costs of health care have led, and may continue to lead, to significant reductions in health care reimbursements. State concerns over the growth in Medicaid expenditures also could result in significant payment reductions. Since these programs generally reimburse on a fee schedule basis, rather than a charge-related basis, we generally cannot increase net revenue by increasing the amount charged for services provided. As a result, cost increases may not be able to be recovered from government payors. In addition, Medicare, Medicaid and other government health care programs are increasingly shifting to forms of managed care, which generally offer lower reimbursement rates. Some states have enacted legislation to require that all Medicaid patients be transitioned to managed care organizations, which could result in reduced payments to us for such patients. Similar legislation may be enacted in other states. In addition, a state-legislated shift of Medicaid patients to a managed care organization could cause us to lose some or all Medicaid business in that state if we were not selected by the managed care organization as a participating provider. Additionally, funds received under all health care reimbursement programs are subject to audit with respect to the proper billing for physician services and, accordingly, repayments and retroactive adjustments of revenue from these programs could occur. We expect that there will continue to be proposals to reduce or limit Medicare and Medicaid reimbursements.

The continued growth of managed care may have a material adverse effect on our business.

The number of individuals covered under managed care contracts or other similar arrangements has grown over the past several years and may continue to grow in the future and a substantial portion of our net revenue is from reimbursement from managed care organizations. Entities providing managed care coverage have been successful in reducing payments for medical services in numerous ways, including entering into arrangements under which payments to a service provider are capitated, limiting testing to specified procedures, denying payment for services performed without prior authorization and refusing to increase fees for specified services. These trends reduce revenues, increase the cost of doing business and limit the ability to pass cost increases on to customers. The continued growth of the managed care industry and increased efforts to reduce payments to medical care providers could materially harm our business.

There have been an increasing number of state and federal investigations of hospitals and hospital laboratories, which may increase the likelihood of investigations of our business practices.

Significant media and public attention has been focused on the health care industry due to ongoing federal and state investigations reportedly related to referral and billing practices, laboratory and home health care services and physician ownership and joint ventures involving hospitals. Most notably, HCA-The Healthcare Company, or HCA, is reportedly under investigation with

respect to such practices. We provide medical director services for numerous hospital laboratories, including 29 HCA hospital laboratories as of March 31, 2002. Therefore, the government's ongoing investigation of HCA or other hospital operators could result in governmental investigations of one or more of our operations. In addition, the OIG and the Department of Justice have initiated hospital laboratory billing review projects in certain states, including some in which we operate, and are expected to extend such projects to additional states, including states in which we operate. These projects further increase the likelihood of governmental investigations of laboratories that we own or operate. Although we monitor our billing practices and hospital arrangements for compliance with prevailing industry practices under applicable laws, such laws are complex and constantly evolving, and it is possible that governmental investigators may take positions that are inconsistent with our practices or industry practices. The government's investigations of entities with which we contract may materially harm our business, including termination or amendment of one or more of our contracts or the sale of hospitals, potentially disrupting the performance of

services under our contracts. In addition, some indemnity insurers and other non-governmental payors have sought repayment from providers, including laboratories, for alleged overpayments.

The heightened scrutiny of Medicare and Medicaid billing practices in recent years may increase the possibility that we will become subject to costly and time consuming lawsuits and investigations.

Payors periodically reevaluate the services for which they provide reimbursement. In some cases, government payors such as Medicare also may seek to recoup payments previously made for services determined not to be reimbursable. Any such action by payors would adversely affect our revenues and earnings. In addition, under the federal False Claims Act, any person convicted of submitting false or fraudulent claims to the government may be required to make significant payments, including damages and penalties in addition to repayments of amounts not properly billed, and may be excluded from participating in Medicare, Medicaid and other government health care programs. Many states have similar false claims laws. The federal government has become more aggressive in examining laboratory billing practices and seeking repayments and penalties allegedly resulting from improper billing for services, such as using an improper billing code for a test to realize higher reimbursement. While the primary focus of this initiative has been on hospital laboratories and on routine clinical chemistry tests, which comprise only a portion of our revenues, the scope of this initiative could expand and it is not possible to predict whether or in what direction the expansion might occur. In addition, recent government enforcement efforts have asserted poor quality of care as the basis for a false claims action. Private insurers may also bring actions under false claims laws and, in some circumstances, private whistleblowers may bring false claim suits on behalf of the government. While we believe that our practices are proper and do not include any allegedly improper practices now being examined, the government could take a contrary position or could investigate our practices. Furthermore, HIPAA and the joint federal and state anti-fraud initiative commenced in 1995 called Operation Restore Trust have strengthened the powers of the OIG and increased funding for Medicare and Medicaid audits and investigations. As a result, the OIG is expanding the scope of its health care audits and investigations. Federal and state audits and inspections, whether on a scheduled or unannounced basis, are conducted from time to time at our facilities. If a negative finding is made as a result of any such investigation, we could be required to change coding practices, repay amounts paid for incorrect practices, pay substantial penalties or cease participating in Medicare, Medicaid and other government health care programs.

In August 2001, we received two letters from the United States Attorney for the Southern District of Ohio (the "U.S. Attorney") requesting information regarding billing practices and documentation of gross descriptions on skin biopsy reports. We provided documentation to the U.S. Attorney regarding the tests that were the subject of its requests for information. Requests for information such as these are often the result of a qui tam, or whistleblower, action filed by a private party relator. In February 2002, we received notification that the U.S. Attorney would not pursue this matter any further. In addition, we were notified that there were then no presently pending lawsuits in the Southern District of Ohio against the Company relating to the request by any private party relator bringing a qui tam action.

We derive a significant portion of our revenues from short-term hospital contracts and hospital relationships that can easily be terminated.

Many of our hospital contracts provide that the hospital or we may terminate the agreement prior to the expiration of the initial or any renewal term with relatively short notice and without cause. We also have business relationships with hospitals that are not subject to written contracts and that may be terminated by the hospitals at any time. Loss of any particular hospital contract or relationship would not only result in a loss of net revenue to us under that contract or relationship, but may also result in a loss of outpatient net revenue that may be derived from our association with the hospital and its medical staff. Any such loss could also result in an impairment of the value of the assets we have acquired or may acquire, requiring substantial charges to earnings. For example, during the fourth quarter of 2000, we were unsuccessful in retaining a contract to perform pathology services for a hospital in South Florida. Based upon the remaining projected cash flow from this hospital network, we determined that the intangible assets were impaired and recorded a pre-tax non-cash charge of approximately $1.0 million. This hospital contract accounted for approximately $800,000 of net revenue during 2000. Continuing consolidation in the hospital industry may result in fewer hospitals or fewer

laboratories as hospitals move to combine their operations. Our contracts and relationships with hospitals may be terminated or, in the case of contracts, may not be renewed as their current terms expire.

Our business strategy emphasizes growth, which places significant demands on our financial, operational and management resources and creates the risk of failing to meet the growth expectations of investors.

Our growth strategy includes efforts to acquire and develop new practices, develop and expand managed care and national clinical laboratory contracts and develop new products, services, technologies and related alliances with third parties. The pursuit of this growth strategy consumes capital resources, thereby creating the financial risk that we will not realize an adequate return on this investment. In addition, our growth may involve the acquisition of companies, the development of products or services or the creation of strategic alliances in areas in which we do not currently operate. This would require our management to develop expertise in new areas, manage new business relationships and attract new types of customers. The success of our growth strategy also depends on our ability to expand our physician and employee base and to train, motivate and manage employees. The success or failure of our growth strategy is difficult to predict. The failure to achieve our stated growth objectives or the growth expectations of investors could disappoint investors and harm our stock price. We may not be able to implement our growth strategy successfully or to manage our expanded operations effectively and profitably.

We are pursuing business opportunities in new markets, such as genomics, which adds uncertainty to our future results of operations and could divert financial and management resources away from our core business.

As we pursue business opportunities in new markets, such as genomics, we anticipate that significant investments and costs will be related to, and future revenue may be derived from, products, services and alliances that do not exist today or have not been marketed in sufficient quantities to measure accurately market acceptance. Similarly, operating costs associated with new business endeavors are difficult to predict with accuracy, thereby adding further uncertainty to our future results of operations. We may experience difficulties that could delay or prevent the successful development and introduction of new products and services and such products and services may not achieve market acceptance. Any failure by us to pursue new business opportunities successfully could result in financial losses and could inhibit our anticipated growth. In addition, the pursuit of new business endeavors could divert financial and management resources away from our core business.

Ethical, social and legal issues concerning genomic research and testing may result in regulations restricting the use of genomic testing or reduce the demand for genomic testing products, which could impede our ability to achieve our growth objectives.

Ethical, social and legal concerns about genomic testing and genomic research could result in regulations restricting our or our customers' activities or in only limited demand for those products. For example, the potential availability of testing for some genomic predispositions to illness has raised issues regarding the use and confidentiality of information obtained from this testing. Some states in the United States have enacted legislation restricting the use of information from some genomic testing, and the United States Congress and some foreign governments are considering similar legislation. The United States Food and Drug Administration, or FDA, has subjected the commercialization of certain elements of genomic testing to limited regulation. The federal Centers for Disease Control and Prevention has published notice of its intent to revise the regulations under the Clinical Laboratory Improvements Amendments, or CLIA, to specifically recognize and regulate a genomic testing specialty. The Department of Health and Human Services' Secretary's Advisory Committee on Genetic Testing advises the Department of Health and Human Services as to various issues raised by the development and use of genomic testing and has published preliminary recommendations for increased participation on the part of the FDA and increased regulation of genomic testing under CLIA. As a result of these activities, it is likely that genomic testing will be subject to heightened regulatory standards. Restrictions on our or our customers' use of genomic information or testing products could impede our ability to broaden the range of testing services we offer and to penetrate the genomic and genomic testing markets.

If we are unable to make acquisitions in the future, our rate of growth could slow.

Much of our historical growth has come from acquisitions, and we continue to pursue growth through the acquisition and development of laboratories and pathology operations. However, we may be unable to continue to identify and complete suitable acquisitions at prices we are willing to pay or to obtain the necessary financing on acceptable terms. In addition, as we become a bigger company, the amount that acquired businesses contribute to our revenue and profits will likely be smaller on a percentage basis. We compete with other companies to identify and complete suitable acquisitions. We expect this competition to intensify, making it more difficult to acquire suitable companies on favorable terms. For example, we may be unable to accurately and consistently

identify operations whose pathologists have strong professional reputations in their local medical communities. Further, we may acquire operations whose pathologists' individual marketing and other sales efforts do not produce a profitable customer base. As a result, the businesses we acquire may not perform well enough to justify our investment.

We may raise additional capital, which could be difficult to obtain at attractive prices and which could cause us to engage in financing transactions that adversely affect our stock price.

We need capital for both internal growth and the acquisition and integration of new practices, products and services. Therefore, we may raise additional capital through public or private offerings of equity securities or debt financings. Our issuance of additional equity securities could cause dilution to holders of our common stock and may adversely affect the market price of our common stock. The incurrence of additional debt could increase our interest expense and other debt service obligations and could result in the imposition of covenants that restrict our operational and financial flexibility. Additional capital may not be available to us on commercially reasonable terms or at all. The failure to raise additional needed capital could impede the implementation of our operating and growth strategies.

The success of our growth strategy depends on our ability to adapt to new markets and effectively integrate newly acquired operations.

Our expansion into new markets will require us to maintain and establish payor and customer relationships and to convert the patient tracking and financial reporting systems of new operations to our systems. Significant delays or expenses with regard to this process could materially harm the integration of additional operations and our profitability. The integration of acquisitions also requires the implementation and centralization of purchasing, accounting, sales and marketing, payroll, human resources, management information systems, cash management, risk management and other systems, which may be difficult, costly and time-consuming. Accordingly, our operating results, particularly in fiscal quarters immediately following an acquisition, may be adversely affected while we attempt to complete the integration process. We may encounter significant unanticipated costs or other problems associated with the future integration into our combined network. Our expansion into new markets may require us to comply with present or future laws and regulations that may differ from those to which we are currently subject. Failure to meet these requirements could materially impede our growth objectives or materially harm our business.

We may inherit significant liabilities from operations that we have acquired or acquire in the future.

We perform due diligence investigations with respect to potential liabilities of acquisitions and typically obtain indemnification with respect to liabilities from the sellers. Nevertheless, undiscovered claims may arise and liabilities for which we become responsible may be material and may exceed either the limitations of any applicable indemnification provisions or the financial resources of the indemnifying parties. Claims or liabilities of acquired and affiliated operations may include matters involving compliance with laws, including health care laws. While we believe, based on our due diligence investigations, that the operations of our operations prior to their acquisition were generally in compliance with applicable health care laws, it is nevertheless possible that such operations were not in full compliance with such laws and that we will become accountable for their non-compliance. We have, from time to time, identified certain past practices of acquired operations that do not conform to our standards. A violation of applicable health care laws, whether or not the violation occurred prior to our acquisition, could result in civil and criminal penalties, exclusion of the

physician, the operation or us from participation in Medicare and Medicaid programs and loss of a physician's license to practice medicine. Significant fines and other penalties could cause liquidity problems and adversely affect our results of operations. Exclusion from participation in government payor programs, which represented 23% of our collections in the first quarter of 2002, would eliminate an important source of revenue and could materially harm our business.

We have significant contingent liabilities payable to many of the sellers of practices that we have acquired.

In connection with our practice acquisitions, we typically agree to pay the sellers additional consideration in the form of contingent debt obligations, payment of which depends upon the practice achieving specified profitability criteria over periods ranging from three to five years after the acquisition. The amount of these contingent payments cannot be determined until the contingency periods terminate and achievement of the profitability criteria is determined. As of March 31, 2002, if the maximum criteria for the contingency payments with respect to all prior acquisitions were achieved, we would be obligated to make payments, including principal and interest, of approximately $140.9 million over the next three to five years. This amount could increase significantly as we continue selectively to acquire new practices. Lesser amounts would be paid if the maximum criteria were not met. Although we believe we will be able to make such payments from internally generated funds or proceeds of future borrowings, it is possible that such payments could cause significant liquidity problems for us. We continue to use contingent notes as partial consideration for acquisitions and affiliations.

We have recorded a significant amount of intangible assets, which may never be realized.

Our acquisitions have resulted in significant increases in net identifiable intangible assets and goodwill. Net identifiable intangible assets, which include hospital contracts, physician client lists, management service agreements and laboratory contracts acquired in acquisitions were approximately $257.1 million at March 31, 2002, representing approximately 41% of our total assets. Net identifiable intangible assets are recorded at fair value on the date of acquisition and are being amortized over periods ranging from 10 to 40 years. Goodwill, which relates to the excess of cost over the fair value of net assets of businesses acquired, was approximately $237.6 million at March 31, 2002, representing approximately 38% of our total assets. On an ongoing basis, we make an evaluation to determine whether events and circumstances indicate that all or a portion of the carrying value of intangible assets may no longer be recoverable, in which case an additional charge to earnings may be necessary. For example, during the years ended December 31, 2000 and 2001, we recorded asset impairment charges to intangible assets in the amount of $9.6 million and $3.8 million, respectively. We may not ever realize the full value of our intangible assets. Any future determination requiring the write-off of a significant portion of intangible assets could materially harm our results of operations for the period in which the write-off occurs, which could adversely affect our stock price.

Our business is highly dependent on the recruitment and retention of qualified pathologists.

Our business is dependent upon recruiting and retaining pathologists, particularly those with subspecialties, such as dermatopathology, hematopathology, immunopathology and cytopathology. While we have been able to recruit, principally through acquisitions, and retain pathologists, we may be

unable to continue to do so in the future as competition for the services of pathologists increases. In addition, we may have to modify the economic terms of our relationships with pathologists in order to enhance our recruitment and retention efforts. Because it may not be possible to recover increased costs through price increases, this could materially harm our profitability. The relationship between the pathologists and their respective local medical communities is important to the operation and continued profitability of each practice. Loss of one of our pathologists for any reason could lead to the loss of hospital contracts or other sources of revenue that depend on our continuing relationship with that pathologist. Our revenues and earnings could be adversely affected if a significant number of pathologists terminate their relationships with our practices or become unable or unwilling to continue their employment, or if a number of our non-competition agreements with physicians are terminated or determined to be invalid or unenforceable. For example, the two pathologists in our Birmingham, Alabama practice recently terminated their employment with us and opened their own pathology lab. As a result, we closed an operating lab in Alabama. We have implemented a strategy to retain those customers and service

them through other AmeriPath facilities, including another lab recently acquired in Alabama. As of December 31, 2001, we had been unable to retain these customers, and therefore recorded a non-cash asset impairment charge of $3.8 million. We continue to aggressively market in Alabama and expect to be successful in gaining some of these customers back during 2002.

Enactment of proposals to reform the health care industry may restrict our existing operations, impose additional requirements on us, limit our expansion or increase our costs of regulatory compliance.

Federal and state governments periodically focus significant attention on health care reform. It is not possible to predict which, if any, proposal will be adopted. It is possible that the health care regulatory environment will change so as to restrict our existing operations, impose additional requirements on us or limit our expansion. Costs of compliance with changes in government regulations may not be subject to recovery through price increases.

Competition from other providers of pathology services may materially harm our business.

Health care companies such as hospitals, national clinical laboratories, third-party payors and health maintenance organizations may compete with us in the employment of pathologists and the management of pathology practices. We also expect to experience increasing competition in the provision of pathology and cytology diagnostic services from other anatomic pathology practices, companies in other health care industry segments, such as other hospital-based specialties, national clinical laboratories, large physician group practices or other pathology physician practice management companies. In particular, national clinical laboratories who presently refer business to us may seek to develop the capacity to do this business in-house. Some of our competitors may have greater financial and other resources than we, which could further intensify competition. Increasing competition may erode our customer base, reduce our sources of revenue, cause us to reduce prices or enter into a greater number of capitated contracts in which we take on greater pricing risks or increase our marketing and other costs of doing business. Increasing competition may also impede our growth objectives by making it more difficult or more expensive for us to acquire or affiliate with additional pathology practices.

We are subject to significant professional or other liability claims, and we cannot assure you that insurance coverage will be available or sufficient to cover such claims.

Our business entails an inherent risk of claims of physician professional liability or other liability for acts or omissions of our physicians and laboratory personnel or of hospital employees who are under the supervision of our hospital-based pathologists. We and our physicians periodically become involved as defendants in medical malpractice and other lawsuits, some of which are currently ongoing, and are subject to the attendant risk of substantial damage awards. While we believe that we have a prudent risk management program, including professional liability and general liability insurance coverage as well as agreements from third parties, such as hospitals and national clinical laboratories, to indemnify or insure us, it is possible that pending or future claims will not be covered by or will exceed the limits of our risk management program, including the limits of our insurance coverage or applicable indemnification provisions, or that third parties will fail or otherwise be unable to comply with their obligations to us. While we believe this practice is routine, in a number of pending claims our insurers have reserved their rights to deny coverage. In addition, we are currently in a dispute with our former medical malpractice carrier on an issue related to the applicability of excess insurance coverage. If we do not prevail, a gap of several months in our excess insurance coverage may exist for a period in which significant claims have been made. It is also possible that the costs of our insurance coverage will rise causing us either to incur additional costs or to further limit the amount of coverage we have. In addition, our insurance does not cover all potential liabilities arising from governmental fines and penalties, indemnification agreements and certain other uninsurable losses. For example, from time to time we agree to indemnify third parties, such as hospitals and national clinical laboratories, for various claims that may not be covered by insurance. As a result, we may become responsible for substantial damage awards that are uninsured. We are currently subject to indemnity claims which, if determined adversely to us, could result in substantial uninsured losses.

The Company was recently notified by its medical malpractice carrier that they will no longer be underwriting medical malpractice insurance and this has placed the Company on non-renewal status effective July 1, 2002. The Company is currently evaluating other potential carriers for medical malpractice and conducting a feasibility study of a captive insurance company. There can be no assurance the

Company will be able to obtain medical malpractice insurance on terms consistent with our current coverage, which may increase our cost.

We depend on certain key executives, the loss of whom could disrupt our operations, cause us to incur additional expenses and impede our ability to expand our operations.

Our success is dependent upon the efforts and abilities of our key management personnel, particularly James C. New, our Chairman and Chief Executive Officer, Brian C. Carr, our President, Gregory A. Marsh, our Vice President and Chief Financial Officer, and Dennis M. Smith, Jr., M.D., our Executive Vice President of Genomic Strategies and Medical Director. It would be costly, time consuming and difficult to find suitable replacements for these individuals. The need to find replacements combined with the temporary loss of these key services could also materially disrupt our operations and impede our growth by diverting management attention away from our core business and growth strategies.

We depend on numerous complex information systems and any failure to successfully maintain those systems or implement new systems could materially harm our operations.

We depend upon numerous information systems to provide operational and financial information on our operations, provide test reporting to physicians and handle our complex billing operations. We currently have several major information technology initiatives underway, including the integration of information from our operations. No assurance can be given that we will be able to enhance existing and/or implement new information systems that can integrate successfully the disparate operational and financial information systems of our operations. In addition to their integral role in helping our operations realize operating efficiencies, such new systems are critical to developing and implementing a comprehensive enterprise-wide management information database. To develop such an integrated network, we must continue to invest in and administer sophisticated management information systems. We may experience unanticipated delays, complications and expenses in implementing, integrating and operating such systems. Furthermore, our information systems may require modifications, improvements or replacements as we expand and as new technologies become available. Such modifications, improvements or replacements may require substantial expenditures and may require interruptions in operations during periods of implementation. Moreover, implementation of such systems is subject to the availability of information technology and skilled personnel to assist us in creating and implementing the systems. The failure to successfully implement and maintain operation, financial, test reports, billing and physician practice information systems could substantially impede the implementation of our operating and growth strategies and the realization of expected operating efficiencies.

Failure to timely or accurately bill for our services may have a substantial negative impact on our revenues, cash flow and bad debt expense.

Billing for laboratory testing services is complicated. The industry practice of performing tests in advance of payment and without certainty as to the outcome of the billing process may have a substantial negative impact on our revenues, cash flow and bad debt expense. We bill various payors, such as patients, insurance companies, Medicare, Medicaid, and national clinical laboratories, all of which have different billing requirements. In addition, the billing information requirements of the various payors have become increasingly stringent, typically conditioning reimbursement to us on the provision of proper medical necessity and diagnosis codes by the requisitioning client. This complexity may increase our bad debt expense, due primarily to several non-credit related issues such as missing or incorrect billing information on test requisitions.

Among many other factors complicating our billing are:

- disputes between payors as to which party is responsible for payment;
- disparity in coverage among various payors; and
- the difficulty of adherence to specific compliance requirements, diagnosis coding and procedures mandated by various payors.

The complexity of laboratory billing also tends to cause delays in our cash collections. Confirming incorrect or missing billing information generally slows down the billing process and increases the aging of accounts receivable. We assume the financial risk related to collection, including the potential uncollectability of accounts and delays due to incorrect and missing information and the other complex factors identified above.

Disruption in New York City and in U.S. commercial activities generally following the September 2001 terrorist attacks on the U.S. adversely impacted

and may continue to adversely impact our results of operations and could adversely impact our ability to raise capital or our future growth.

The operations of our laboratories were and may continue to be harmed by terrorist attacks on the U.S., like the one in New York City. For example, transportation systems and couriers that we rely on to receive and process specimens have been and may continue to be disrupted, thereby causing a decrease in testing volumes and revenues. In addition, we may experience a rise in operating costs, such as costs for transportation, courier services, insurance and security. We also may experience delays in receiving payments from payors that have been affected by attacks, which, in turn, would harm our cash flow. The U.S. economy in general may be adversely affected by the terrorist attacks or by any related outbreak of hostilities. Any such economic downturn could adversely impact our results of operations, impair our ability to raise capital or impede our ability to continue growing our business.

Our stock price is volatile and the value of your investment may decrease for various reasons, including reasons that are unrelated to the performance of our business.

There has been significant volatility in the market price of securities of health care companies that often has been unrelated to the operating performance of such companies. In fact, since January 1, 2000, our common stock, which trades on the NASDAQ National Market, has traded from a low of $7.00 per share to a high of $37.16 per share. We believe that various factors, such as legislative and regulatory developments, investigations by regulatory bodies or third-party payors, quarterly variations in our actual or anticipated results of operations, lower revenues or earnings than those anticipated by securities analysts, the overall economy and the financial markets could cause the price of our common stock to fluctuate substantially. For example, in the fourth quarter of 1998, our stock price declined significantly as a result of an announcement by the government of its intent to seek recovery of amounts allegedly improperly reimbursed to us under Medicare. Although the claim was resolved to our satisfaction and resulted only in a small fine, similar investigations may be announced having the same effect on the market price of our stock. In addition, securities class action claims have been brought against companies whose stock prices have been volatile. Several such suits were brought against us, and subsequently dismissed, as a result of the decline in our stock price described above. This kind of litigation could be very costly and could divert our management's attention and resources. Any adverse determination in this type of litigation could also subject us to significant liabilities, any or all of which could materially harm our liquidity and capital resources.

Certain provisions of our charter, by-laws and Delaware law may delay or prevent a change of control of our company.

Our corporate documents and Delaware law contain provisions that may enable our board of directors or management to resist a change of control of our company. These provisions include a staggered board of directors, limitations on persons authorized to call a special meeting of stockholders and advance notice procedures required for stockholders to make nominations of candidates for election as directors or to bring matters before an annual meeting of stockholders. We also have a rights plan designed to make it more costly and more difficult to gain control of our company. These anti-takeover defenses could discourage, delay or prevent a change of control. These provisions could also discourage proxy contests and make it more difficult for you and other stockholders to elect directors and cause us to take other corporate actions. In addition, the existence of these provisions, together with Delaware law, might hinder or delay an attempted takeover other than through negotiations with our board of directors.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

INTEREST RATE RISK

We are subject to market risk associated principally with changes in interest rates. Interest rate exposure is principally limited to the amount outstanding under the credit facility of $97.0 million at March 31, 2002. Currently the balances outstanding under the credit facility are at floating rates. Based on the outstanding balance of $97.0 million, each quarter point increase or decrease in the floating rate changes interest expense by $242,000 per year. In the future, the Company may evaluate entering into interest rate swaps, involving the exchange of floating for fixed rate interest payments, to reduce interest rate volatility.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

During the ordinary course of business, the Company has become and may in the future become subject to pending and threatened legal actions and proceedings. The Company may have liability with respect to its employees and its pathologists as well as with respect to hospital employees who are under the supervision of the hospital based pathologists. The majority of the pending legal proceedings involve claims of medical malpractice. Most of these relate to cytology services. These claims are generally covered by insurance. Based upon investigations conducted to date, the Company believes the outcome of such pending legal actions and proceedings, individually or in the aggregate, will not have a material adverse effect on the Company's financial condition, results of operations or liquidity. If the Company is ultimately found liable under these medical malpractice claims, there can be no assurance that the Company's medical malpractice insurance coverage will be adequate to cover any such liability. The Company may also, from time to time, be involved with legal actions related to the acquisition of and affiliation with physician practices, the prior conduct of such practices, or the employment (and restriction on competition of) physicians. There can be no assurance any costs or liabilities for which the Company becomes responsible in connection with such claims or actions will not be material or will not exceed the limitations of any applicable indemnification provisions or the financial resources of the indemnifying parties.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

There were no shares of Common Stock issued in the first three months of 2002. In April 2002, the Company issued 11,570 shares of stock in connection with the Empire Pathology acquisition.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K AND 8-K/A

(a) Reports on Form 8-K and 8-K/A

A Current Report on Form 8-K, dated April 4, 2002, was filed by the Company with the Securities and Exchange Commission on April 4, 2002, reporting that on April 1, 2002, the Audit Committee of AmeriPath, Inc. recommended to its Board of Directors and the Board of Directors approved the engagement of Ernst and Young as its independent auditors for the year ending December 31, 2002 to replace the firm of Deloitte & Touche LLP (Deloitte). Deloitte was dismissed on April 1, 2002 as auditors of the Company effective upon the completion of the required procedures and communications in connection with Deloitte's audit of the financial statements

for the year ended December 31, 2001. The reports of Deloitte on the Company's financial statements for the past two years did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope, or accounting principles. In connection with the audits of the Company's financial statements for each of the two years in the period ended December 31, 2001, and in the subsequent interim period, through the date of Deloitte's termination on April 1, 2002, there were no disagreements with Deloitte on any matters of accounting principles or practices, financial statement disclosure, or auditing scope and procedures which, if not resolved to the satisfaction of Deloitte, would have caused Deloitte to make reference to the matter in their report. The Company had requested Deloitte to furnish it a letter addressed to the Commission stating whether it agrees with the above statements. A copy of that letter, dated April 12, 2002 is filed as Exhibit 16 to the Form 8-K A.

The current report on Form 8-K, dated April 4, 2002, was subsequently amended on a current report on Form 8-K/A, dated April 1, 2002, as filed by the Company with the Securities and Exchange Commission on April 15, 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERIPATH, INC.

Date: May 14, 2002

By: /s/ JAMES C. NEW

James C. New
Chairman and Chief Executive Officer

Date: May 14, 2002

By: /s/ GREGORY A. MARSH

Gregory A. Marsh
Vice President and
Chief Financial Officer