

## Executive Summary

██████████ has been in the drug testing and background checking business for 14 years. The owners wish to retire and move on to other things in life including helping their son in his business.

██████████ is a subchapter S corporation, 84% held by ██████████ and 16% by her husband ██████████. As with all companies dependent on the general economy, they were hurt significantly by the general economic downturn and they restructured the business to survive it. Since the bulk of their revenue is dependent upon hiring, the lack of hiring since 2008 has hurt the business. On the other hand, the increase in hiring anticipated in the post-recession era means a great future. Also, as a third party administrator in the industry, other people in the business, including the labs, need ██████████ and those like them.

The company has three major activities: Drug testing and background checks in the ██████████ area, the same on a national level and serving as a Third Party Administrator the industry including medical review as required by law. ██████████ enjoys an excellent reputation and serves its customers with a full range offering, good serves and 24/7 on-line service availability.

██████████ serves four primary market segments: Medical and Health Services, the Staffing Industry, the Transportation Industry and general industry. The majority of revenue is from the medical sector in large part because they are a third party administrator.

██████████ has a strong customer base with excellent customer relationships. With minimal sales effort combined with an improving economy and better promotion of their background checking product the company can achieve substantial growth.

After growing to multiple locations in the ██████████ and in ██████████, the worldwide economic recession took a major toll on the business. By resizing to a single location and selling off the ██████████ operation, the business now earns more operating income with dramatically less sales and less overhead, selling and administrative expenses.

## **Business Summary**

### **Background**

██████████ has its roots in the drug testing and background checking industry beginning in 1998. Originally formed as ██████ Drug and Alcohol Testing as a sole proprietorship, in May of 2000 they reformed into ██████ a subchapter S corporation. The company was founded by ██████ as a local operation soliciting business in the ██████ region using the instant result testing devices newly approved by the state legislature. As the company evolved they developed a more national scope and added elements including management program development, third part administration, medical review and sophisticated systems to manage on a national level.

The company is currently located at ████████████████████. Prior to the economic recession of 2008, ██████ had collections locations scattered around the ██████ area. The ██████ Street location is in a small office complex near ████████████████████ and centrally located for the ██████ region close to uptown and with easy access to local businesses and expressway access.

█████ is one of the few companies in the market able to provide a full range of services and the entire process from collection through medical review. As a Third Party Provider (TPA), they are able to provide background checks, POCT, lab testing, drug program management, third party collections, transportation permits testing, and medical review services.

### **Management**

██████████: President and 84% ownership share, worked in banking and insurance sales prior to starting this business. ██████ has led the sales effort since the beginning and trained many others in the industry who have opened local operations in other cities. At 58 years old ██████ plans to semi retire but is likely to get involved in clinical blood testing, a business opened several years ago by ██████. It is unrelated to drug testing.

██████████: General Manager and 16% owner, married to ██████. ██████ has worked in banking as an EVP in commercial lending for 25 years. ██████ joined the business four years ago when ██████ retired from commercial banking. ██████ intends to fully retire and devote time to the charitable organizations in which ██████ is currently involved.

### **Market Overview**



The drug and background testing sector has been evolving over the past 10 to 15 years. It is driven by several key trends that continue to gain momentum in the marketplace and long term drive business to [REDACTED] and its competitors. Most significant is the desire by employers and many laws and regulations requiring employers to drug test and background test their employees. In addition a number of national and local laws and regulations require testing and background checking. Recent examples of new requirements were the drug testing of taxi driver for the recent airport taxi contract in [REDACTED] and requirements of drug testing and background checking workers in transportation (DOT), nursing homes, day care centers and restaurants. Although the testing techniques may evolve, the demand is expected to grow well into the future. Frankly, once a company begins using drug testing it is highly unlikely they would stop doing so.

The market is served in a variety of ways. It is comprised primarily of small local companies serving local markets with collection and program management. These firms typically serve local accounts and support them outside of the area with collections through local labs. Typically, a local firm has an arrangement with one of a handful of labs such as Lab Corp. or Quest Diagnostics. They complete tests and are often contracted for collections when not being done directly by the drug testing company.

To understand the market dynamics, one first has to understand the risks. Since this is part of the hiring process and random drug testing is a job requirement, errors carry a high risk. A wrong test result can cost someone their job or block them from being able to get a job. As a result the process requires control and absolute certainty in the result. This means separation of responsibilities such that a positive or failed test must be reviewed by a third party. The lab which obtained the result under federal regulatory rules cannot use its own doctor to review the results. The process is divided into five key elements:

1. Collection: This can be completed or accomplished by a local collection site or a local collector. Often drug testing companies collect their own and use labs such as Lab Corp or Quest to collect outside of their local areas. It is not uncommon for local clinics and urgent care centers to the collection although they are not typically cost effective.
2. Lab Test: Any number of national or local labs can complete the testing and report the results. Serve to certify test results under federal regulatory rules. [REDACTED] maintains relationships with all testing laboratories to assure they can provide the proper test needed for a client. Tests can be completed with a standard urine test, a hair test or with a blood test. Generally this is the preference of the employer and the test v. time factors they wish to use. Most local collection sites will not offer a blood test option. As with all medical matters, this information is kept highly confidential and submitted to the drug testing firm.



3. **Medical Review:** For positive tests, a certified medical review officer must review the test result and contact the individual involved. Certified officers are MDs who have been through special training for drug test review. They are required to review the result and either agree or disagree including discussing the result with the individual to identify any unusual circumstances which may explain the result.
4. **Secured Reporting:** With confidential information that is also bound by HIPPA laws, security is critical. Test results have to be carefully guarded with access limited to only authorized individuals. As a result secure computer systems with limited access are a requirement. The systems in this industry are critical for security and record retention.
5. **Record Retention:** TPAs play an important role in record retention and access by clients. Legal compliance issues required maintaining records for five years. Although rare, clients do need access to results for a number of years. In essence these become a permanent part of an employee's record.

Although some market consolidation is expected, we are not aware of any efforts to roll up the industry. To date it is scattered with many small firms serving local markets, a few firms with broader and national reach like [REDACTED] but no dominating or exceptionally large national player. There are several modest size competitors in Charlotte with the largest being Wolfe Drug Testing and [REDACTED] being somewhat smaller but [REDACTED].

As the economy improves and drug testing revenue returns to 2008 and pre-recession levels, the revenue should quickly grow. Further drug and background testing continues to be legislated into hiring processes. Incidents and backlash from incidents in schools, hospitals, taxi cabs and restaurants has caused state legislators to mandate tests and checks for certain jobs. Interestingly, it is a matter of cost and risk reduction for employers if they can say the drug tested and background checked their employees they can reduce their insurance premiums and reduce their liability in the event of an unfortunate incident involving their employee and others.

## Product Overview

The product offering of is readily divided into five key categories: drug testing, TPA of drug testing, background testing, medical review and other lab tests.

- **Drug testing:** Far and away the largest part of the business at [REDACTED]. This is distributed among three categories: instant, Non DOT testing, and DOT testing. 69% of the testing is non-DOT while 16% is for DOT testing and the balance is instant testing. Instant



testing only indicates very recent drug usage. For example urine tests are good at testing recent drug usage in a three day or so window while saliva tests only check within a 24 to 36 hour window. These tests tend to be used by companies looking to rely on low cost and quick result. Laboratory test for DOT and non-DOT are both highly accurate and shows recent 3 plus days for most drugs but for marijuana it shows use for up to a 45 day drug usage period. In either case, a failed drug test requires further medical review and analysis.

- **Drug testing by type:** There are three primary forms of drug tests with varying levels of results. ■■■ conducts drug tests of the following types:
  - Instant: The test is conducted from a saliva or urine sample and can be used for pre-employment testing only in most states. Experience indicates the instant test are accurate for showing negative results, but can show false positives and therefore any positive result must be confirmed by a certified laboratory. These tests are the test of choice for some companies due to fast results and low cost.
  - Urine laboratory test: This is the most common test and will indicate recent drug usage with accuracy for 3 days on some illicit drugs and longer for others. The test results reports drug families in its results lending itself to Medical Review with minimal risk of a false positive.
  - Hair laboratory test: This test indicates drug use over a longer period of up to 120 days. ■■■ takes a hair sample which is tested for drug use. Like the urine test, it reports drug families facilitating medical review. This test looks back approximately four months based on the standard testing length of 1.5 inches.
- **TPA of drug testing:** ■■■ serves a key role in drug testing by providing medical review for other firms who obtain a positive test result. Using a robust computer system that allows for confidential submittal and reporting, they provide medical review for other drug testing firms. They also will do collections for other firms in their local operation.
- **Background checking:** Although not sold separately, ■■■ provides background checks on the individuals they drug test when requested by clients. There are other firms in the industry who focus on background checking. These reports can be bought on-line. ■■■ buys theirs as required. Other players in the industry do their own checking in their state by accessing various government and credit agency web sites, while contacting others to do checks outside of their area.
- **Other lab tests:** although not common, ■■■ is occasionally asked to do DNA testing required for use in litigation and also serves as a collection and reporting site. The company is capable of any testing not requiring them to draw blood.

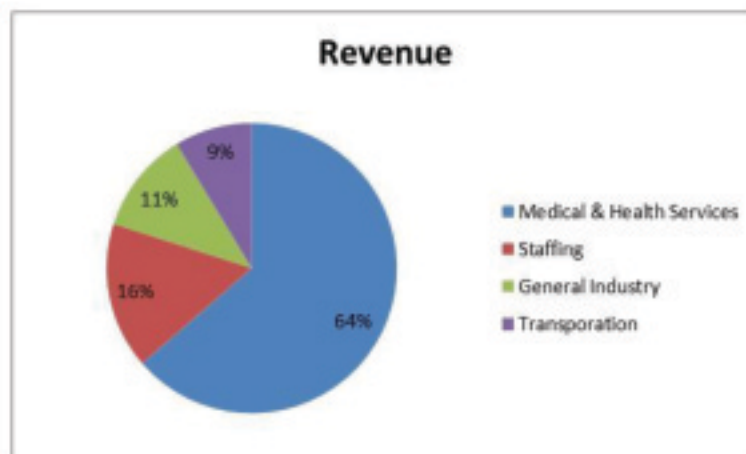
## Sales Overview

■■■ has been the primary sales driver for ■■■ over the years. Although they have had additional sales people, currently ■■■ handles it all. The company has excellent customer relationships. They are in contact with most customers on a regular basis and keep

abreast of all issues. They have an active prospecting activity looking for significant sales opportunities in underserved areas. [REDACTED] generates local business through his contacts and charitable activities in the region while [REDACTED] works on national and more significant opportunities.

[REDACTED] actively promotes their services for screening applicants. They put emphasis also on random drug testing and sell this service heavily. They will structure the random testing program for customers and administrate for them as needed. This is critical for customers to keep the programs compliant with labor laws as well as make them effective.

While [REDACTED] sells to wide variety of companies, their revenue can be sorted among four primary categories: Staffing Agencies, Medical and Health Service Organizations, Transportation and General Manufacturing and Service Companies.



As you can see in the pie chart, the medical segment is today's biggest segment. It is the result of significant revenue from labs and healthcare for the Third Party Administrator portion of [REDACTED]. Also, as would be expected in the recent economy, the medical sector remained strong while staffing, general hiring and transportation were depressed. It historically has been 50% of revenue.

Although no one customer tends to dominate the business, revenue for each customer tends to vary year to year by market conditions and their own hiring activity and practices. The ranking of top customers tends to change each year. Below is a chart showing revenue by the top 15 customers since 2007 or pre-recession through 2011.



Customer	<u>Revenue By Customer</u>				
	2007	2008	2009	2010	2011
A	104,054.50	154,985.50	111,450.50	97,273.00	79,793.90
B	20,346.00	22,667.40	23,962.00	20,535.50	36,032.60
C	490	812.5	2,493.00	44,380.00	32,791.50
D	7,167.00	16,219.80	20,597.80	32,509.00	28,657.40
E	24,920.00	7,782.30	10,322.50	36,361.00	28,519.40
F		57,965.00	38,631.00	38,961.00	26,595.00
G	32,453.61	14,397.67	10,676.45	20,322.50	23,773.85
H	13,488.91	22,894.90	24,357.90	30,429.00	20,252.50
I		11,074.00	15,691.00	13,026.00	18,468.00
J	2,283.00	25,760.00	12,930.00	15,420.00	17,433.20
K	9,852.00	11,306.60	10,192.90	12,089.00	13,954.20
L	14,071.00	6,659.50	1,107.70	3,573.90	12,978.90
M	6,453.00	4,466.30	3,561.80	4,944.20	10,648.90
N	14,043.63	12,754.80	16,756.60	15,480.70	8,970.80
O	7,100.00	6,750.00	11,303.00	8,911.00	7,987.00

As you can see, there have been no significant lost customers in the past five years. A little better attention to sales activity would have generated new customers and the owners recognize both the missed opportunity but also the potential a little sales effort can generate.

## Outlook

Naturally as the economy improves employers will start hiring more people and thus add to the volume at █. The majority of drug tests and background checks are for new hires by employers of all types. More significant, █ is in a strong position to grow even more as a result of their status as a third party administrator and because the demand for drug testing and background checking is growing. Oddly, while corporate America began drug testing in the 1990s, much of retail and other sectors of society were not testing.

Additional opportunity for growth is in the background checking sector. This has become much more important in society. Also, it has been under-promoted by █ until the last six months. Background checks are easily done and readily passed through with a markup. For convenience most customers wish to have both services provided by one supplier. With more effort and emphasis put on sales and a product offering of bundled drug tests and background checks the outlook for █ is for significant growth.

## Earnings

Although revenue declines have been the norm through the recession, profitability is surprisingly good. With 2011 revenue of \$604K, operating margins were 56% and EBITDA was 35% prior to owner's salary and draw. Historically, much of earnings were lost in the multiple locations [REDACTED] operated and owner's salary and draw were minimized for tax purposes while [REDACTED] was working outside of this business.

Over the past four years, [REDACTED] has right sized to current market needs and requirements selling and closing their other locations and making more use of outside collection services. This included closing multiple locations in the general [REDACTED] area and the [REDACTED] as well as selling off their operations in [REDACTED]. These costs are included in the results below when they occurred. The result has been good earnings on lower sales and significantly lower costs. Their remote location in [REDACTED] was sold at the end of 2010.

GlobalLab Solutions, Inc.						
Profit & Loss						
	2006 to 2011					
	2006	2007	2008	2009	2010	2011
Net Sales/Revenue	\$614,282	\$1,217,217	\$1,266,724	\$805,461	\$739,967	\$604,325
Cost of Goods Sold	\$326,911	\$682,665	\$629,734	\$360,072	\$346,044	\$263,066
Gross Margin	\$287,372	\$534,553	\$636,990	\$445,388	\$393,923	\$341,259
SG&A	\$228,346	\$438,949	\$561,253	\$359,490	\$231,874	\$128,868
EBITDA Prior to Officer Salaries	\$59,026	\$95,604	\$75,737	\$85,898	\$162,049	\$212,391

## Appendix