

# Catholic Health Initiatives Signs Pact with PAML

► **Goal is to pursue hospital lab joint ventures in multiple regional markets served by CHI hospitals**

►► **CEO SUMMARY:** *In concept, it is a simple deal. Catholic Health Initiatives (CHI), the nation's second largest Catholic health system, is taking a 25% equity position in Pathology Associates Medical Laboratories (PAML). However, the consequences may be significant. PAML now has an open door to develop laboratory joint ventures with the 78 hospitals operated by CHI. It also is positioned to become the primary esoteric and reference testing partner for the CHI hospitals.*

**T**HERE'S A NEW INVESTOR AND PARTNER at Pathology Associates Medical Laboratories (PAML) of Spokane, Washington. It's a business move that positions this regional laboratory powerhouse to expand nationally.

Last Tuesday, **Providence Health & Services** of Seattle, Washington, which owns PAML, announced a new agreement with **Catholic Health Initiatives (CHI)** of Denver, Colorado. CHI will assume a 25% equity position in PAML.

This deal brings together two big health systems. Providence operates 27 hospitals and 35 non-acute care facilities in the western United States. Catholic Health Initiatives is the nation's second largest Catholic health system. It operates 78 hospitals and 40 non-acute care facilities in 20 states. CHI has annual revenue of \$6.8 billion.

Laboratory testing services are at the heart of this unprecedented new business relationship. Both Providence and CHI recognize the importance of further expanding their clinical services in the outpatient/outreach sector. For outreach laboratory testing, both health systems will utilize PAML as one vehicle to accomplish that goal.

The new agreement between Providence and Catholic Health Initiatives benefits PAML in three ways. First, it creates access for PAML to establish laboratory testing joint ventures with CHI's 78 hospitals in 20 states. In turn, this may help PAML become a national laboratory organization. That's because CHI's hospitals are located in states ranging from Washington and Oregon on the west coast, all the way to Pennsylvania, New Jersey, and Maryland on the east coast.

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R. Lewis Dark, Founder & Publisher.

Robert L. Michel, Editor.

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Second, with Catholic Health Initiatives as an equity owner, PAML gains improved access to the capital it needs to expand. This is an important benefit, since it is difficult for an operational unit of a not-for-profit health system to raise money by borrowing or selling equity.

### ► Reference Testing Source

Third, the agreement positions PAML to become a primary source of reference testing for CHI's 78 hospitals. Not only would this contribute to seamless service in laboratory joint ventures between PAML and CHI hospitals, but it would create an opportunity for PAML to market itself more widely as a national reference laboratory.

"With the agreement finalized, we expect the next steps will quickly take place," noted Noel Maring, Senior Vice President and Chief Marketing Officer at PAML. "For example, market studies and joint venture business plans involving specific CHI hospitals are already in place. Implementation at these laboratory joint venture sites is ready to begin immediately.

"At this time, PAML expects to have operational laboratory joint ventures in 10 new markets within the next 36 to 48 months," explained Maring. "This demonstrates the confidence our new partner has in the strategy of using lab outreach testing to expand its presence in the outpatient/outreach marketplace. It also positions PAML for rapid growth."

### ► Lab's Strategic Value

At its core, the significance of the new agreement between Providence and Catholic Health Initiatives is the strategic value of laboratory testing. For pathologists and clinical lab administrators, this development affirms that some health system administrators recognize how their hospitals can leverage outreach laboratory testing to achieve a wider strategic objective.

"Both Providence Health and Catholic Health Initiatives recognize the strategic necessity of expanding their clinical services

into the outpatient and outreach sectors," stated Maring. "Since 1980, annual growth in outpatient procedures has been at double digit rates, compared to single-digit growth rates in inpatient procedures.

"It means the largest number of patients never get to the hospital, but are seen in doctor's offices and similar ambulatory settings," he continued. "Innovative health systems understand that success in the future will come from being able to provide a continuum of care that includes outpatient and ambulatory services as well as inpatient services.

"For hospitals that want to build clinical service bridges into these outreach environments, laboratory testing is a proven strategy," observed Maring. "This is why Catholic Health Initiatives recognized how a laboratory joint venture can support and advance this strategy.

### ► Established Track Record

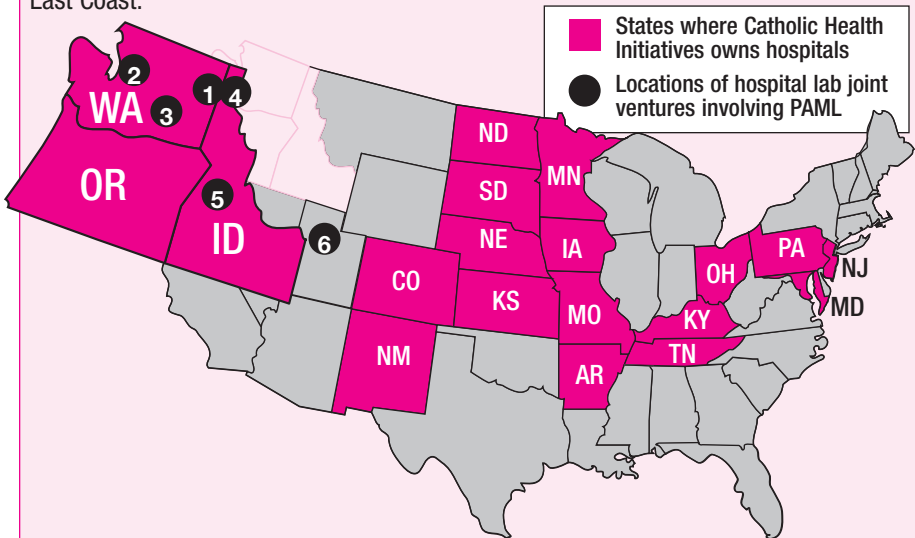
"Further, when it comes to establishing and operating lab testing joint ventures with hospitals that generate substantial cash flow to the hospital partner, PAML has a track record that is unmatched over the past 15 years," added Maring.

"In our lengthy discussions and negotiations with CHI officials, it was clear that they understand how laboratory joint ventures can help individual hospitals achieve wider strategic goals," he said. "These extend beyond the substantial revenue and cash flow produced by a successful, growing hospital lab outreach program.

"A well-run laboratory outreach testing program helps the hospital forge tighter professional relationships with physicians in the community," explained Maring. "It also introduces an electronic lab test ordering and results reporting capability between the hospital and the physicians' offices. This electronic link is often used to allow the physician to access other information systems within the hospital."

# Deal with Catholic Health Initiatives Positions PAML to Grow into a National Laboratory

**T**HIS MAP IDENTIFIES THE EXISTING LOCATIONS where Pathology Associates Medical Laboratories operates hospital laboratory outreach joint ventures. The six operational laboratory joint ventures are found in Washington, Idaho, and Utah. The 20 states shown in color identify where Catholic Health Initiatives (CHI) operates hospitals. This map illustrates why PAML now has the potential to become a national laboratory. That's because CHI operates hospitals in states that include the West Coast, the Rocky Mountains, the Midwest, the Midsouth, and the East Coast.



## PAML's Existing Joint Ventures with Hospital Labs

- 1 PAML**  
 Spokane, WA—Founded 1990  
 Providence Sacred Heart Medical Center
- 2 PACLAB NETWORK LABS, LLC**  
 Olympia, Tacoma, Seattle, Everett, Bellevue, Kirkland, Renton, WA—Founded 1996  
 PAML (Bellevue, Seattle, Olympia)  
 Providence Health System—Washington  
 Providence Everett Medical Center  
 Providence Centralia Medical Center  
 Franciscan Health System  
 St. Josephs Medical Center  
 St. Francis Hospital  
 St. Clare Hospital  
 Stevens Healthcare  
 Evergreen Healthcare  
 Overlake Hospital & Medical Center  
 Valley Medical Center
- 3 TRI-CITIES LABORATORY, LLC**  
 Kennewick, Pasco, Richland, WA—Founded 1997  
 Lourdes Health Network  
 Kennewick General Hospital  
 Kadlec Medical Center
- 4 ALPHA MEDICAL LABORATORY, LLC**  
 Coeur d'Alene, ID—Founded 1995  
 Kootenai Medical Center
- 5 TREASURE VALLEY LABORATORY**  
 Boise, ID—Founded 1999  
 Saint Alphonsus Regional Medical Center
- 6 MOUNTAINSTAR CLINICAL LABS, LLC**  
 Salt Lake City, UT—Founded 2007  
 St. Marks Hospital  
 Lakeview Hospital  
 Ogden Regional Medical Center

In fact, sophisticated use of information technology (IT) is one secret behind the success PAML has demonstrated in developing, operating, and sustaining multiple laboratory outreach programs with different hospitals over the past 15 years. PAML believes that sophisticated use of information technology (IT) is a powerful way to differentiate its laboratory services from other lab competitors in the market.

“That is true,” responded Maring. “Our laboratory joint ventures with hospitals are organized around two principles. One, the hospital laboratory should emphasize its core competency, which is lab testing. Two, PAML should provide all the support services that wrap around the actual step of performing the test.

“That means PAML provides and manages everything but the actual testing itself,” he added. “This division of duties plays to the strength of each partner in the lab joint venture.

### ► Soup To Nuts JV Support

“PAML is responsible for sales, marketing, courier services, customer services, coding, billing, collections, and reporting on operational performance,” stated Maring. “Next comes our trump card. We have an informatics backbone that links these functions to the hospital laboratory, the hospital LIS, and the client physicians served by the outreach program.

“PAML has invested heavily to build this informatics platform. It supports every aspect of laboratory operations and service,” noted Maring. “We took **Microsoft Corporation’s** Customer Relationship Management (CRM) software product and customized it for the unique needs of a clinical laboratory. All our different software systems in the lab interface with the CRM.

“This home-grown informatics solution is called Joint Venture Advantage,” he continued. “It will be an integral part of each laboratory joint venture developed with Catholic Health Initiatives.

“Keep in mind that JV Advantage gives our joint venture labs a ‘high touch’ capability,” stated Maring. “We consistently perform at a 5+ Sigma level in many functions at our laboratory. Five Sigma means 230 defects per million events.

### ► Competitive Advantage

“Because most competing labs still struggle to operate at 3 or 4 Sigma—66,800 and 6,210 defects per million events, respectively—our outreach physician clients quickly recognize the superior service we provide. In turn, that generates competitive advantage to our hospital lab joint venture,” commented Maring.

Lab administrators and pathologists should not underestimate the potential of PAML’s new agreement with Catholic Health Initiatives. PAML has a proven track record in creating and operating dynamic hospital laboratory joint ventures. These JVs consistently return ever-growing cash flow back to the hospital partner. They also contribute to reduced inpatient testing costs because of the growing test volume.

For its part, Catholic Health Initiatives offers 78 hospitals located in 20 states as potential joint venture partners. As Maring noted, based on development work already completed prior to the signing of the agreement, PAML expects the CHI relationship will allow it to expand into 10 new regional markets over the next 36 to 48 months.

### ► Potential For More Lab JVs

Plus, CHI is not the only iron in the PAML fire. PAML is now ending the second full year of its hospital laboratory joint venture with **MountainStar Healthcare Network** in Salt Lake City, Utah, a health system owned by **Hospital Corporation of America (HCA)**. (See *TDRs*, December 10, 2007 and March 3, 2008.) It would not be a surprise if the success of the MountainStar JV encouraged other HCA hospitals to initiate a laboratory joint venture with PAML.

**TDR**  
Contact Noel Maring at 509-755-8946 or nmaring@PAML.com.