

*Celebrating 10 years  
of Service to the  
Laboratory Industry!*



*From the Desk of R. Lewis Dark...*

# THE **RD** **DAIRK** **REPORT**

RELIABLE BUSINESS INTELLIGENCE, EXCLUSIVELY  
FOR MEDICAL LAB CEOs/COOs/CFOs/PATHOLOGISTS

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**R. Lewis Dark**

**Founder & Publisher**



## ***Do Regional Laboratories Have A Bright Future?***

IF INTEGRATED INFORMATICS CAPABILITIES will be a major point of differentiation among competing laboratories in the future, then several warning flags have recently appeared in the laboratory industry. Regional laboratories and hospital lab outreach programs should take notice.

One warning flag is the recent announcement by **Laboratory Corporation of America** that “eLabCorp,” a Web-connectivity system is ready for market. According to LabCorp, the system is more than a lab test ordering/lab test resulting product. It also “integrates easily with a wide variety of existing electronic medical record and practice management systems, allowing doctors to access the Web for testing services without changing the computer services they use for the rest of their practice needs.”

Another warning flag is a deal just disclosed by **Quest Diagnostics Incorporated** in early September that calls for **North Texas Specialty Physicians** of Fort Worth, Texas, an IPA with 600 physicians, to use Quest Diagnostics’ “Care360” physician portal. It is a Web-enabled system that “enables doctors to order diagnostic tests and review laboratory tests online; prescribe medication at the point of care; view clinical and administrative information from multiple sources; file documents received electronically or in hard copy into a health record; and share confidential patient information with medical colleagues in a manner that is consistent with HIPAA (Health Insurance Portability and Accountability Act) privacy and security requirements.”

A third warning flag is the success of **Bio-Reference Laboratories, Inc.** (BRLI) at using enhanced informatics capabilities to build its regional laboratory business and develop high-value lab testing niches. (*See pages 9-15.*) BRLI may be further along in the development of a multi-function informatics system than any laboratory in the world, at this moment.

The themes of these three warning flags could not be clearer. To gain competitive advantage, three of the nation’s largest lab companies are investing heavily in information technologies. They all have the same goal: to make it easier and simpler for physicians to order lab tests, access test results, and integrate laboratory information in their electronic medical record systems. Regional labs should take heed and develop their own integrated informatics solution, in conjunction with local health systems. **TDR**

# Our Tenth Anniversary Serving Your Needs

*THE DARK REPORT marks ten years  
of providing business intelligence*

**CEO SUMMARY:** *It was on September 25, 1995 that the first issue of THE DARK REPORT was published. The laboratory industry was in financial turmoil. There was widespread consolidation in both the commercial lab sector and among hospital laboratories. Reimbursement for lab testing services was falling rapidly. Yet, through all these negative changes, there were still opportunities for growth and financial success.*

**By Robert L. Michel**

**I**T'S AN ANNIVERSARY we feel justifies a headline! With this issue, THE DARK REPORT celebrates ten years of service to the laboratory industry.

Our first issue was dated September 25, 1995. It arrived on the scene as the laboratory industry—reeling from the effects of gatekeeper HMOs, along with contracts built around capitated reimbursement and full utilization risk to laboratory providers—was approaching its financial nadir.

In the commercial laboratory sector, 1995 was the year that **MetPath, Inc.** was a \$1.7 billion giant and changing its name to **Corning Clinical Laboratories**. In April 1995, **Roche Biomedical Laboratories** acquired **National Health Laboratories** and adopted a

new name: **Laboratory Corporation of America**. With \$1.4 billion in revenues, LabCorp passed **SmithKline Beecham Clinical Laboratories** (\$1 billion) to become the nation's second largest lab company.

Things were similarly chaotic in the hospital laboratory sector. 1995 marked the start of a remarkable 45-month cyclone of hospital mergers and acquisitions. By December 31, 1998, **SMG Marketing Group** of Chicago, Illinois was reporting that the nation now had 604 integrated health systems (IHSs), a 50% increase in IHSs during that time. According to SMG, these IHSs owned, controlled, or managed 3,760 of the country's 4,838 general, non-federal acute care hospitals. This was an 83% increase from the 2,060

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hospitals that were in IHSs in April, 1995! (See *TDR*, April 5, 1999.)

Of course, consolidation of hospital ownership had a huge impact on hospital laboratories. The years 1995 through 2000 were marked by a huge number of projects to consolidate and integrate laboratory services across all the hospitals within an IHS.

And if that wasn't enough, soon Congress would pass the 1997 Balanced Budget Act (BBA). This legislation drastically reduced the amount of Medicare money flowing to hospitals in the following few years, generating even more severe financial pressure on hospital laboratories.

### Helping Lab Leaders

It was during these chaotic times for all laboratories that THE DARK REPORT arrived on the scene with a simple goal: to provide laboratory administrators and pathologists with the type of reliable business intelligence that would make an immediate difference in the financial and operational success of their laboratory organizations.

In fact, our lead story in the September 25, 1995 issue featured the strategic thinking of Paul Mango, who was Executive Director of the **Reference Laboratory Alliance** (RLA) at that time. This 40-hospital regional laboratory network, based in Pittsburgh, was attracting national attention throughout the laboratory industry.

As a laboratory business model, RLA had two primary objectives. The first goal was to engage hospital laboratories in Greater Pittsburgh to collaborate in negotiating patient access for lab outreach programs from the area's **Blue Cross/Blue Shield** insurer. The second goal was to create an integrated laboratory testing infrastructure—linked by sophisticated information technology services—that would enable the community hospital's lab

outreach program to compete effectively against the national laboratories.

In this story, THE DARK REPORT emphasized three specific strategic imperatives Mango recommended for hospital-based laboratories. They were:

- The economic posture of hospital-based laboratories must improve if they are to survive.
- The necessary economic improvement in hospital labs cannot be achieved without growing the revenue base [by using outreach testing programs].
- The revenue base of hospital laboratories cannot increase substantially (and, in fact, will continue to decrease) without participation in managed care contracts.

Ten years later, Mango's strategic analysis remains relevant, notwithstanding the disappearance of the gatekeeper-model HMO from the healthcare marketplace in recent years. In providing this intelligence to our readers in 1995, THE DARK REPORT was arming them with accurate intelligence to guide their laboratory organizations through the financial turmoil that beset the entire lab industry over the balance of that decade.

### Hospital Lab Outreach

Today, estimates are that 50% or more of the nation's hospitals operate some type of laboratory testing outreach program. This is graphic evidence that Mango's strategic imperatives in 1995 were accurate guidance for lab directors and pathologists.

Over the past ten years, THE DARK REPORT has worked hard to identify emerging market trends and provide intelligence about the successes enjoyed by early-adopter laboratories and pathology group practices. We were first to predict that exclusive

national lab testing contracts with big insurers would be problematic—both for the laboratory winning the contract and the insurer.

In our November 13, 1995 issue, we analyzed the recently-announced, and first-ever, sole-source national lab testing contract between SmithKline Beecham Clinical Laboratories (SBCL) and **Cigna Corporation**. Worth an estimated \$100 million per year to SBCL, it was our prediction that such pacts would not only be difficult to make work effectively, but would fail to deliver the promised financial benefits to all parties while alienating a large number of physicians providing care to Cigna patients.

### Impact Of Deep Discounts

All of that came true, and more. During the next three years, SBCL aggressively pursued, and won, a number of sole-source national lab testing contracts by offering deeply-discounted prices. During those same years, Corning Clinical Labs (now **Quest Diagnostics Incorporated**) and LabCorp began to show pricing discipline in contract negotiations with major payers.

During 1997 and 1998, while average revenues-per-requisition were increasing at Quest Diagnostics and LabCorp, they were declining at SBCL. THE DARK REPORT believes SBCL's deteriorating financial performance during those years played a major factor in motivating its parent company, **SmithKline Beecham Plc**, to sell its lab business to Quest Diagnostics during 1999.

I tell this story for a reason. It illustrates why accurate and timely business intelligence, as presented on these pages, helps lab executives and pathologists make more informed business decisions.

## Where Is He Now? Update on Paul Mango

IN RECOGNITION OF THE TENTH ANNIVERSARY OF THE DARK REPORT, it seems appropriate to do our first "Where Are They Now" update on the subject of the lead story in the inaugural issue of THE DARK REPORT, published on September 25, 2005.

That lead story featured the strategic thinking of Paul Mango, who was then employed by the **Institute for Transfusion Medicine** in Pittsburgh and was the Executive Director of the Regional Laboratory Alliance (RLA). As a lab executive, Mango had a unique background. He is a graduate of the **United States Military Academy at West Point** in New York, holds an MBA from **Harvard University**, and was employed by **McKinsey & Company**, one of the world's most-respected strategic business consultants, prior to his position at the Institute for Transfusion Medicine.

The 40-hospital RLA broke apart over the next 24 months as the competing integrated health systems (IHSs) of **UPMC Health System** and **Allegheny Health System** acquired community hospitals and, after the acquisition, pulled the laboratories of the acquired hospitals out of the Reference Laboratory Alliance. Around this time, Mango returned to work at McKinsey & Associates.

Since that time, Paul Mango has developed special expertise in strategic consulting on healthcare issues for some of the nation's leading organizations and corporations. THE DARK REPORT caught up with Mango just two weeks ago in Tucson, Arizona. Mango was there to co-facilitate a lab industry strategic "think tank" underwritten by **Sysmex Corporation**.

Still a keen strategic thinker on healthcare issues, Mango's advice to lab executives and pathologists is to expect consumer-directed health plans (CDHPs) to rapidly have a major impact on the American healthcare system. Mango says this is good news for labs, because it will allow them to re-establish direct business relationships with both referring physicians and patients.

For example, the passage of time demonstrated that the handful of locally-owned, pathologist-managed lab companies that operated through the balance of the 1990s always continued to make money—because they had the discipline to not bid for managed care contracts that reimbursed lab testing at marginal cost.

***Some executives of these labs have told us, over the years, that our analysis of events, and our coverage of these types of stories, provided them with both the knowledge and the confidence they needed to stay out of the deeply-discounted and/or capitated lab contracting fracas.***

Some executives of these labs have told us, over the years, that our analysis of events, and our coverage of these types of stories, provided them with both the knowledge and the confidence they needed to stay out of the deeply-discounted and/or capitated lab contracting fracas. They were comfortable losing access to managed care patients, while concentrating on the remaining—and much smaller—market of fee-for-service patients.

With the attainment of our tenth anniversary publishing THE DARK REPORT, we think it's timely to introduce two new features. In future issues, we will reach back ten years, pull out an important lab industry story of that time, and assess its impact then and now.

Much of the information we have presented on these pages contains management wisdom which never goes out of date. There are some fascinating “old” stories which have new lessons to teach, even as they validate

the original points we were striving to make at that time.

To complement this retrospective analysis of a major story of past years and its continuing influence on the present, we would like to introduce an occasional feature called “where are they now?” We will search out individuals who were influential in the laboratory industry during those years, but then vanished from the scene. You will get an update on what's happened to them, plus a dollop of their current advice to the lab industry—but only if they have something relevant to say.

To launch this new feature, check out the sidebar on the previous page. It's an update on Paul Mango, who was the subject of the lead story in our first issue of THE DARK REPORT on September 25, 2005. Having caused a stir in the lab industry back then with his leadership in designing, implementing, and operating a 40-hospital regional laboratory network in Pittsburgh, no one should be surprised that Mango is once again poised to shake up the healthcare world.

This time his message is that consumer-directed health plans will stimulate major changes to the American healthcare system. But then, that's a story we've already written about in THE DARK REPORT earlier this summer. (*See TDR, July 11, 2005.*)

## **Ten Eventful Years**

In closing, all of us at THE DARK REPORT would like to express our thanks for your support during these ten eventful years. You have welcomed us into your labs as we've traveled across the country. You've shared your strategies, your secrets, and your setbacks with us. It's helped us to better understand what's working...and what's not in lab management. **TDR**  
Contact Robert Michel at 512-264-7103.



# AmeriPath Will Acquire Specialty Laboratories

*AmeriPath is changing strategies, will emphasize reference/esoteric testing*

**CEO SUMMARY:** *It's a surprise to most lab industry observers. AmeriPath, a company built around 400 anatomic pathologists working mostly in community hospitals, is acquiring a national reference/esoteric testing company. However, this deal may be better understood by looking at the motives of Welsh, Carson, Anderson & Stowe, the private equity firm which owns AmeriPath.*

**W**HAT AN UNLIKELY COMBINATION! AmeriPath, Inc. is buying Specialty Laboratories, Inc. At first glance, there doesn't seem to be a compelling economic or business argument to marry an anatomic pathology services company with a national reference/esoteric lab company.

The sale was announced late last Friday, September 30. AmeriPath will pay \$13.25 per share for all 23.8 million outstanding shares of Specialty Labs, for an estimated total of \$314.7 million.

Founder James Peter, M.D., Ph.D., along with his family and a trust, will receive approximately \$66 million in cash from the sale. They will also invest \$119 million for a 20% equity position in AmeriPath after the acquisition closes. Peter has controlled about 60% of Specialty Lab's stock since its IPO in December 2000.

Subject to regulatory clearance of the acquisition, AmeriPath expects the sale to close in early 2006, making Specialty Laboratories a private company. AmeriPath has stated that the lab

facility operated by Specialty Laboratories in Valencia, California will remain open and is likely to receive additional specimens after the acquisition.

## Struggling Businesses

As most clients and regular readers of THE DARK REPORT know, in recent years, both Specialty Laboratories and AmeriPath have struggled with different business problems. In the case of Specialty Laboratories, it stabilized its core business following the loss of its Medicare license in April 2002. But the move into the Valencia laboratory facility last December increased the company's overhead. It has not generated enough new sales to offset its higher operating costs and generate adequate profits.

The primary business challenge at AmeriPath is how to spark—and then sustain—strong growth in specimens, revenues, and operating profits in its hospital-based anatomic pathology group practices. In recent years, a succession of insiders have told THE DARK REPORT that the costs of running

these pathology groups, particularly pathologist salaries, have risen much faster than either revenues or profits.

On the other hand, AmeriPath has two profitable and rapid-growing business lines. One involves dermatopathology services and the other is AmeriPath's reference and esoteric testing services, anchored by its Center for Advanced Diagnostics in Orlando, Florida.

## Uninterested Buyers

THE DARK REPORT is also aware that, as AmeriPath has shopped itself to potential buyers, these buyers were very interested in the dermatopathology and esoteric testing businesses, but expressed little interest in buying the hospital-based pathology business.

Herein lies the key to understanding AmeriPath's pending acquisition of Specialty Laboratories. In recent months, AmeriPath has actively reorganized itself into three business units: dermatopathology, reference/esoteric testing, and hospital-based anatomic pathology services.

AmeriPath's owner, **Welsh, Carson, Anderson & Stowe**, needs an exit strategy. The reorganization of AmeriPath into three distinct business lines—two of which are highly attractive to buyers like **Quest Diagnostics Incorporated** and **Laboratory Corporation of America**, provides a hint as to AmeriPath's strategic thinking.

## To Improve Profit Margins

Now comes the decision to spend one-third of a billion dollars to acquire Specialty Laboratories. (But remember, Peter is investing \$119 million of that number into the post-merger AmeriPath.) The business logic may be that AmeriPath's volume of reference and esoteric testing, when switched to Specialty's Valencia laboratory, can improve the profit margins on Specialty's core business.

Further, having reference laboratory capability on both coasts will allow the Specialty and AmeriPath sales teams to increase the rate of new sales, thus feeding more specimens into the Valencia facility.

Fast forward a couple of years. Now AmeriPath has a profitable national business in reference and esoteric testing. The test mix is highly attractive to Quest Diagnostics and LabCorp because it is a blend of hospital-referred specimens (tested mostly in Valencia) and high-end esoteric anatomic pathology specimens (tested mostly in the Orlando laboratory).

## Welsh Carson's Motives

Seen from the perspective of Welsh Carson, this is a viable exit strategy. If they consider their original investment in AmeriPath to be a lemon, then acquiring Specialty Laboratories is a way to make lemonade. This would be equally true of the Specialty shareholders. Alone, Specialty faced several more years of struggle to raise specimen volumes high enough to offset its overhead.

This scenario still misses one point. What happens to the anatomic pathology group practices that were acquired by AmeriPath? Informed sources tell THE DARK REPORT that one potential solution is to sell these groups back to the pathologists, at an attractive price. These sources say the steady rumors about discontented employee-pathologists have plenty of substance. So this strategy would be win-win for AmeriPath and for the pathologists.

Is this a reasonable business scenario? The dots seem to connect in a consistent way. However, it requires effective execution from the management of AmeriPath and Specialty Labs. At a minimum, THE DARK REPORT believes this acquisition is the result of intractable weaknesses within both companies. That will make the next few years at AmeriPath interesting to watch. **TDR**



## Informatics Update

# GE Healthcare Will Acquire IDX Systems for \$1.2 Billion

*IDX's physician office management system helps GE position itself for the universal EMR*

**B**IG CORPORATIONS continue racing to create the universal EMR (Electronic Medical Record) and a fully-integrated healthcare informatics platform.

Last Thursday, September 29, **General Electric Co.** announced that it would pay \$1.2 billion to acquire **IDX Systems Corporation** of Burlington, Vermont. The transaction is expected to close in early 2006.

Executives from both companies touted the deal as an ideal marriage. The core business at IDX is selling both physician medical groups and hospitals software for billing, scheduling, and electronic medical records. GE Healthcare has strengths in radiology, image archiving, and PACS.

### Doctor Groups & Hospitals

Although not the largest player in the market, IDX includes among its clients more than 850 medical group practices and 500 hospitals in 370 integrated delivery networks. Long known for billing and scheduling solutions, only in recent years has IDX entered the market for electronic medical records.

It was in 2003 that GE Healthcare purchased **Triple G Systems Group, Inc.** of Toronto, Canada. GE Healthcare was interested in the laboratory information system sold by Triple G. At the time of the acquisition, one GE executive had noted that "because

most clinical treatment decisions are based on laboratory test results, the potential for improving patient safety by enhancing workflow in this area is significant."

Since the Triple G acquisition, GE Healthcare has continued to acquire software products that will allow it to build an integrated healthcare informatics platform. "We believe the acquisition of IDX fits nicely in GE Healthcare's portfolio of next generation healthcare businesses; with **Amersham**, its recent predictive diagnostics acquisition, GE can likely now predict, diagnose, inform and treat patients far sooner and with higher degrees of accuracy than in the past," wrote **Prudential** analyst Nicholas Heymann in a research note.

THE DARK REPORT observes that GE Healthcare is just one of several major corporations, like **Motorola** and **IBM**, that are developing major informatics solutions for healthcare. Collectively, these companies want to offer software products that create clinical value by presenting the clinician with a full and complete patient record, then offering him/her recommendations for treatment generated by proprietary algorithms.

For laboratories and pathology groups, this has the potential to interpose another layer between the laboratory and the referring physician. **TDR**

## Nation's Largest Mid-Size Lab Firm Thinks Local and Acts Global

# *Bio-Reference Labs Develops Regional & Niche Strategies*

**I**N AUGUST, two of the nation's mid-size laboratory companies were acquired. The sale of **LabOne, Inc.** and **Clinical Pathology Laboratories, Inc.** puts **Bio-Reference Laboratories, Inc.** (BRLI) in a unique position.

It is the largest laboratory company serving office-based physicians that is not owned by a billion-dollar parent. With sales projected at \$160 million for this year, BRLI, based in Elmwood Park, New Jersey, now occupies the gap between the nationals and smaller independent labs. Over the past five years, the company has enjoyed annual revenue growth of 20.39%.

### **Strong Rate of Growth**

In recent years, BRLI has posted strong rates of growth in specimen volume, revenues, and earnings. Bio-Reference Labs considers itself a laboratory that responds to unmet needs—some regional, some national. It has a deliberate strategy of seeking out specific markets in diagnostic testing that offer value-added opportunities and can provide it with competitive advantage.

This is why lab administrators and pathologists should study BRLI's business strategies. Its dual focus on regional and national opportunities offers insights into strategies a local laboratory can use to gain competitive advantage over

**CEO SUMMARY: Bio-Reference Laboratories, Inc. (BRLI) of Elmwood Park, New Jersey is a lab company on a roll. In just five years, it has grown from \$66 million to more than \$160 million in annual revenues. For regional laboratories across the country, BRLI's business strategies demonstrate how a well-focused business plan, combined with good management execution, can generate sustained increases in specimen volume, revenues, and profit margins. In this exclusive interview, BRLI CEO Marc Grodman, M.D. shares details about BRLI's strategies and success.**

national labs in the regional healthcare community it serves.

"BRLI is probably the most misunderstood lab company operating today," stated Marc Grodman, M.D., President of BRLI. "This is true for two reasons. One, most lab managers and pathologists consider BRLI to be a somewhat traditional lab, providing primarily routine testing services to office-based physicians. Two, within the investment community, the unorthodox nature of BRLI's business strategy makes it a more complex company to study and understand."

BRLI's primary market is highly competitive. It serves physician offices, nursing homes, and clinics in the greater New York City area. This metro area spans eastern New York, Connecticut, New Jersey, and Pennsylvania. The company also offers

services in certain specialized, focused markets that are national in scope.

"We've built our growth strategy around two key themes," noted Grodman. "One is to find innovative, targeted opportunities in diagnostic testing. The other is to offer personalized service to our physician-clients."

### **Hyper-Competitive Market**

"Today's lab marketplace is both rapidly changing and hyper-competitive," he continued. "Innovation drives competitive advantage. Small labs are capable of innovating at a swift pace. That allows them to offer clinicians unique services which may not yet be available from competing labs."

"Match this innovation with personalized service and regional companies like BRLI are perfectly positioned to drive

volume growth and enjoy strong customer loyalty. That translates into high rates of client retention," explained Grodman.

"National laboratory companies enjoy an enormous advantage because of economies of scale," observed Grodman. "This allows the national labs to enter just about any market using discounted pricing. On the other hand, they've grown so large that they are challenged to deliver the kind of personalized services physicians and patients want. This creates significant opportunities for us, as it does for any regional or niche/specialty laboratory."

"Differentiation and service are the reasons why BRLI is not like the majors," he said. "We are a retail lab, not a wholesaler. BRLI represents a different type of business plan. We are a regional lab that looks for focused market opportunities—markets that are unique in some way. Some may be non-traditional markets that are developed locally and then attract business nationally."

"BRLI looks for lab testing segments that have two primary attributes," explained Grodman, "First, by providing services tailored to the unique needs of clients, BRLI differentiates itself from any other laboratory competitor. Second, the lab testing and other primary services can be sold at a 'retail' price because of the added value BRLI provides to clients."

As a laboratory, we want to compete on value and generate higher margins.

“By developing focused testing businesses—creating a series of lab testing franchises, if you will—BRLI not only grows, but it earns better margins on the resulting business. This gives us the cash flow to invest in the next round of testing segments we want to develop,” observed Grodman.

### **Start Local, Expand National**

As Bio-Reference Labs builds a lab testing segment locally, it is also looking for opportunities to capture clients in other geographical markets. “We’ve learned how to maximize our growth potential in our core market, which includes the greater New York area and reaches into Connecticut, New Jersey and parts of Pennsylvania,” Grodman observed. “But, we also recognize that growth potential in a defined regional market has its limits.

“Our segment strategy allows us to find a segment of the lab marketplace where we can differentiate ourselves from the competition—and be paid at retail,” he continued. “Once we’ve developed this business segment locally, we have the resources, the experience, and the sales and marketing team to introduce our services into other regions around the country.

### **Different Business Model**

“This is the part of our business model which is not understood by many people,” added Grodman. “BRLI offers different services in different segments of the lab testing marketplace. A laboratory company is not defined by its test menu, but by the market it serves. You are your demographics.”

BRLI believes that niche markets alone are not enough to sustain double digit rates of growth over the years. “Another rich area for gaining competitive advantage is to anticipate customers’ needs. When it comes to per-

sonalized customer service, quality and quantity are inversely proportional,” observed Grodman. “This works to the advantage of those smaller regional and local laboratories capable of providing innovative, high-quality services at competitive prices, while maintaining the human ‘connectivity’ factor.

“A regional lab can offer very intense personal services and connection with the community it serves,” he continued. “It is easy for local pathologists to visit with local physician-clients. After all, lab testing involves laboratory medicine and physicians do value a personal relationship with a knowledgeable pathologist. It is not easy for pathologists in the national labs to have such personal contact with local physician-clients. At BRLI, we build our business around these advantages.”

### **Lab Tests & Informatics**

Grodman offers several examples of these business lines. “Genpath is an outstanding cancer and genomics laboratory that is national in scope; it is probably the finest hematopathology lab in the country,” he said. “We have a steadily-expanding correctional health program. Our PSIMedica business unit offers clinical knowledge management services. It can aggregate disparate data—including claims data, enrollment data, prescription data, and laboratory data—and produce an array of information solutions for reducing healthcare costs and improving quality performance.

“Many hospital outreach programs are aware of CareEvolve, which is our Web-based healthcare portal,” he noted. “We sell a version of CareEvolve as a comprehensive connectivity solution to physicians and laboratories nationwide. CareEvolve is now used at 18 hospitals and hospital systems around the country. It serves over 100,000 patients. Our ability to provide advanced services are tightly-interwoven around our technology investment in CareEvolve.

# Bio-Reference Laboratories Posts Strong, Multi-Year Rates of Growth

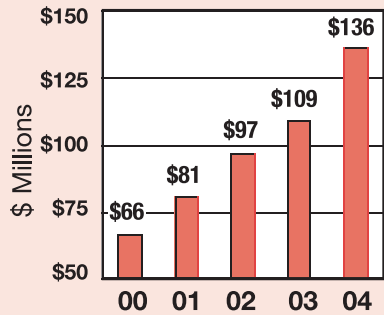
**BRL** Bio-Reference Laboratories, Inc.

**N**OW THE NATION'S LARGEST MID-SIZE LAB COMPANY, Bio-Reference Laboratories, Inc. (BRL) is projected to generate more than \$160 million in annual revenues for its fiscal year, which ends October 31, 2005. As the two graphs show, the company's growth in annual revenues and net income has been substantial since 2000.

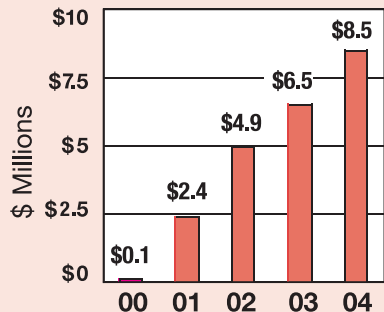
## Bio-Reference Labs At-A-Glance

- **Founded** ..... 1981
- **Headquarters** ..... Elmwood Park, NJ
- **2005 Revenues** ..... >\$160 million (est.)
- **Business Lines** ..... Lab tests for MD offices,  
..... Lab tests for prisons  
..... GenPath (*oncology*)  
..... PsiMedica (*info services*)  
..... CareEvolve (*connectivity*)
- **Employees** ..... 819 full-time/337 part-time
- **CEO** ..... Marc Grodman, M.D.
- **CIO** ..... Richard L. Faherty
- **COO** ..... Howard Dubinett
- **CFO** ..... Sam Singer
- **CMO** ..... James Weisberger, M.D.
- **Sr. VP, Sales/Marketing** ..... Charles T. Todd

## Annual Revenues



## Net Income



“BRLI is what you might call a ‘super-regional’ lab company,” said Grodman. “Superimposed on this platform, we build franchises in multiple areas that benefit from our basic infrastructure and strong marketing staff. Our strategic focus is to develop ways to provide value-added lab services to physicians and healthcare providers. We seek out areas where we can make a difference. We enter market segments where we see the opportunity to add value.

“Our correctional health contracts represent one example of the segment franchise strategy,” he explained. “During this past quarter, we were selected as a primary labo-

ratory vendor for **Correctional Medical Services**. Based in St. Louis, Missouri, it is a major player in the national market for correctional health. We are using the experience we’ve gained in our correctional health testing contracts with the City of New York and the New York State Corrections Department to expand into other regions.”

One element which attracted BRLI’s attention to the correctional market is the test mix. “Prison populations need HIV and HCV testing,” observed Grodman. “These are higher-revenue tests. It fits with our strategy of seeking market opportunities with potential for higher revenues per patient.

“However, correctional testing contracts cannot be simply considered as another ‘lab account.’ Correctional institutions need multiple testing capabilities and require specific analytical support. These are high-service clients in the fullest sense of the term,” observed Grodman.

“As a regional laboratory, we were willing to develop the infrastructure to service the specific needs of correctional clients,” he added. “However, as we developed this ability and gained experience servicing this niche, we’ve built the business infrastructure which gives us the ability to establish this same service model in other states. We now provide correctional health laboratory services in New Mexico, Kansas, and Maine. We believe these are examples of market segments that regional laboratories need to develop if they are going to compete effectively over time.

“Another market segment we are developing is oncology,” noted Grodman. “In particular, we think the surgical pathology subspecialty of hematopathology has particular promise.

### **Growing Oncology Market**

“This is based on our experience. BRLI has enjoyed robust growth in top-line revenues across all lines of business,” he observed. “However, the greatest growth has been in our oncology revenues. Oncology testing tends to be more intense because it is such a rapidly evolving area.

“We want BRLI to be the source of clinical expertise, meaning that we offer the referring clinician more than just a set of numbers from the test result,” commented Grodman. “In oncology, technology advances in both therapeutics and diagnostics are exploding. If we have access to tissue; that is, if BRLI has diagnosed the original tissue, we can go back to the refer-

ring physician and discuss the appropriateness of additional testing and the relationship of this testing to potential therapies—some so new that the clinician may not be fully aware of them and their relevance for his/her patient.”

Essentially, Grodman is describing a market segment model, this time in oncology, which moves the pathologist closer to the clinician as a medical consultant. This tight clinical relationship anchors the client to BRLI and means that a competitor offering a lower price for a test is not likely to cause this client to switch to a competing laboratory.

### **Oncology Sales Force**

Evidently BRLI is making this particular business strategy succeed. “Our oncology business is expanding rapidly,” he said. “Every day, we perform as many bone marrow procedures as any lab in the country. We believe we have one of the best hematopathology laboratories in the country. Oncology diagnostics is one area where we have been able to make a real difference for our clients. We support this business segment with a dedicated sales force, advanced reporting techniques, academic-style reporting, and state-of-the-art clinical practices.”

If there is any single strategy that underpins all aspects of BRLI’s business lines, it is advanced informatics capabilities. “All lab directors and pathologists understand that, in simplest terms, a laboratory is basically an information company,” emphasized Grodman. “For a laboratory, this means it is necessary to interweave informatics into any business opportunity it wants to exploit. I consider informatics to cover the sciences concerned with gathering, manipulating, storing, retrieving and classifying recorded information. Such a broad description reminds us that informatics requires a variety of resources to func-



tion effectively in support of the lab and its clients.”

“This is why we believe the underlying basis of productivity at any lab is informatics. For a long time, many lab managers and pathologists have failed to fully appreciate how sophisticated use of informatics can add tremendous value to their laboratory testing services,” observed Grodman.

“Moreover, the current effort to establish a national healthcare information system is a timely warning for all labs and pathology groups,” he added. “It shows how the inescapable momentum leading us to a different healthcare system is informatics-driven.”

Grodman, who actively participates in laboratory industry lobbying efforts in Washington, D.C., believes the drive to better use healthcare informatics creates major opportunities for laboratories. “In D.C., the hottest thing right now is pay-for-performance,” stated Grodman. “All pay-for-performance programs are based on data warehousing and analytical processing.

“Data warehousing provides the capability to analyze large amounts of historical data. For health organizations, like laboratories, with large quantities of information, this can result in significant competitive advantage,” explained Grodman. “It enables multiple-user and aggregate queries that cut across different segments of a company's operation.

### Combining Data Sets

“As one example, regional testing data could be compared against physician subspecialty data, even if they were originally stored in different databases with different structures,” he continued. “It’s an efficient way to manage and report on data that is from a variety of sources, non-uniform, and scattered throughout the healthcare organization.

“Online analytical processing (OLAP) uses database tables to enable multidimensional viewing, analysis,

## Potential Business Niche Emerging in Histology

**H**ISTOLOGY IS A SLICE of the lab marketplace which is on the Bio-Reference Laboratories’ (BRLI) radar screen.

“This is a lab specialty which interests us,” stated Marc Grodman, M.D., CEO of BRLI. “We believe hospitals will find it increasingly difficult to compete in histology, for several reasons.

“First, it is getting more difficult to hire skilled histotechnologists,” he explained. “Second, the explosion of new histology procedures increases the complexity of running a histology laboratory with a broad menu—particularly if the hospital cannot generate enough specimen volume to justify new, in-house histology services.

“As histology becomes more complex and requires more capital investment, we think that a market for outsourcing certain histology services will emerge,” he observed. “This is a perfect niche for a regional laboratory like BRLI.

“We have the infrastructure to provide this service. We have expertise in running a sophisticated histology laboratory. And we have the ability to recruit, retain, and support both histotechs and pathologists with subspecialty expertise. For us, histology represents an exciting business opportunity,” concluded Grodman.

and querying of large amounts of data,” noted Grodman. “This technology enables management to get fast answers to complex queries, or to analyze historical data for trends and patterns. There are only a handful of analytical engines in the U.S.”

Bio-Reference Laboratories has one of these analytical engines. “We believe ours may be the simplest, easiest, and most intuitive,” declared Grodman. “We’ve done 15 imports from major medical companies. Within five to ten



years all labs will be part of pay-for-performance programs. Laboratory data will be critical to care. It will be linked to reimbursement. Laboratories need to make a strategic decision about how they will be part of this process.”

### Value-Added Informatics

Bio-Reference Labs is moving forward with its informatics strategy. “Success at BRLI is based on pinpoint market analysis enabled by sophisticated information technology,” stated Grodman. “We expect pay-for-performance programs will cause Medicare and private payers to more closely monitor outcomes—and to use detailed information about clinical practices to help providers improve patient outcomes. We believe BRLI already has as much relevant information as any other healthcare provider to support this effort.

“In fact, we saw the benefits from our informatics platform in the weeks following Hurricane Katrina,” offered Grodman. “After Katrina passed through parts of Louisiana, Mississippi, and Alabama, we found it tough to deliver test results to client-physicians in the affected areas.

### Remote Access Via Web

“However, as physicians and some oncology patients undergoing therapy relocated into unaffected areas, using the Internet, they were able to access our system to retrieve both current test results and their cumulative test records,” recalled Grodman. “This allowed treatments to continue with minimal disruption. Laboratory services like this made a difference in the lives of these patients. It was also a powerful demonstration of how a laboratory’s informatics capability creates recognizable value for physicians and their patients.

“This sophisticated informatics capability was not achieved over-

night,” advised Grodman. “It’s taken almost 15 years for Bio-Reference Laboratories to build up its informatics infrastructure.

“During these same years, many independent lab companies disappeared from the market. BRLI survived and thrives today because it never viewed itself in the traditional way, as a clinical laboratory organized to deliver test results to referring physicians. Rather, we’ve operated from a deeper, more sophisticated understanding of the role of laboratory testing in the healthcare system,” observed Grodman.

### Prediction Is Now Fact

“In fact, it was 2000 when I spoke at the *Executive War College*, in detail, about this business vision. We were actively shaping BRLI into a knowledge-based entrepreneurial enterprise, built around a customer-connectivity business model. It’s all IT-based,” he said. “Now, in 2005, BRLI is exactly where we predicted it would be in 2000!”

THE DARK REPORT makes two observations about BRLI. First, it provides a valid example of how regional laboratories can build their own profitable lab testing business from a value-added business strategy. As Grodman pointed out, local laboratories must sell their services at ‘retail’ because of the price advantage enjoyed by national lab companies. But to sell at retail, the lab must offer services that have value to client-physicians and which cannot be easily duplicated by competing labs.

Second, BRLI demonstrates that it is possible for a regional laboratory to build national lines of business, using the infrastructure and capabilities originally created to serve a local market. **TDR**  
Contact Marc Grodman, M.D. at 201-791-2600.

—By Pamela Scherer McLeod

# WSJ Slams Client Bill For Lab Test Services

*Reporter scrutinizes client bill arrangements for lab services in GI, dermatology, and urology*

**CEO SUMMARY:** *In a front-page story last Friday, the Wall Street Journal published an investigative story on the topic of client billing for laboratory testing and anatomic pathology services. It's a "must-read" story for all pathologists and lab managers. For years, the lab industry has recognized how client-billing arrangements can encourage a variety of abuses and illegal practices.*

**Q**UITE POSSIBLY THE COMPLIANCE RISK WAS JUST RAISED for physicians participating in client bill arrangements and/or in-house diagnostic/lab testing services.

On Friday, September 30, 2005, the *Wall Street Journal* (WSJ) published a front-page story titled "Lucrative Operation—How Some Doctors Turn a \$90 Profit From a \$17 [Lab] Test." The reporter analyzed lab testing arrangements between pathologists and referring dermatologists, gastroenterologists, and urologists.

The story contained detailed examples of how such arrangements can generate considerable profit to the referring physician—while at the same time giving that same physician an economic incentive to order unnecessary tests because of the profit they generate. THE DARK REPORT recommends that lab executives and pathologists obtain a copy of this story and study it carefully.

In recent months, the *Wall Street Journal* has investigated different ways that office-based physicians can

profit from ancillary services. On May 2, 2005, it published a story on in-practice radiology arrangements. The themes were two. These arrangements were driving up payer costs because office-based physicians performed more radiology procedures on their patients. Second, legitimate questions have been raised about the quality of radiology services provided by office-based physicians, most of whom have never trained specifically in radiology and related medical procedures.

## **WSJ Alerted By Pathologists**

It was the publication of this story on potential abusive practices in radiology that led the *Wall Street Journal* to laboratory testing. Several pathologists called the reporter and alerted him to similar situations involving clinical laboratory testing and anatomic pathology services. Over the course of the summer, this reporter has dug deeply into this subject.

THE DARK REPORT considers it significant that the September 30 story concentrates on client billing arrangements and builds its case primarily

from dermatology and dermatopathology arrangements. Because of the high-volume nature of skin biopsy analysis, this is the subspecialty within pathology that has most frequently used client-billing arrangements to attract new dermatology accounts.

### Client Billing In Dermpath

The *WSJ* story provides such an example involving **Laboratory Corporation of America**. The *WSJ* story describes how LabCorp offered a Tennessee dermatologist a \$30 client-bill price for a skin biopsy in 2004, a procedure reimbursed at \$109 per biopsy by **Blue Cross/Blue Shield of Tennessee**. This would generate a profit of 265% for each biopsy case submitted by the dermatologist to the insurer. In another instance, where “a Nashville doctor group was charged only \$17 for a biopsy analysis,” a LabCorp spokesman had characterized that price level as an “outlier.”

The *WSJ* notes that LabCorp estimates that 10% of its \$3 billion in annual revenues comes from client-bill types of arrangements. **Quest Diagnostics Incorporated** told the *WSJ* that approximately 6% to 7% of its \$5.1 billion in annual revenues are from client-bill accounts.

### Pathology Laboratories

Pathologist-owned laboratories were also scrutinized in the story. **National Dermatopathology Laboratory** of Lake Balboa, California was mentioned as offering client-bill arrangements with physicians in other states. **Lakewood Pathology Associates** of Lakewood, New Jersey, was identified as having done a presentation at the **American Urological Association** meeting in San Antonio, Texas last summer, promoting a “revenue share model” that would allow referring urologists to generate up to \$35,000 annually.

THE DARK REPORT believes publication of this story by the *Wall Street Journal* is significant for several reasons. First, the *Wall Street Journal* played a major role during the 1980s in exposing poor quality and fraud in certain laboratories around the country. The resulting publicity stimulated Congress to pass legislative reform, including the Clinical Laboratory Improvement Act of 1988 (CLIA). This series of stories has the potential to turn up the heat on Congress and government health regulators to address the abuses in client-bill and physician self-referral arrangements involving laboratory testing and other diagnostic services.

### Changing Standards?

Second, the simple fact that the *WSJ* is pursuing this topic in a series of unfolding stories can be interpreted as a sign that the ethical standards expected of physicians by the American public are rising. Even if many of these client-bill arrangements meet the letter of today’s law, it is likely that growing numbers of consumers find them abusive. This is a subject of concern to consumers, which is precisely why the *WSJ* is publishing stories on this topic.

Third, there is a slim chance that the publication of these stories, now and in the near future, will stimulate federal healthcare investigators to actively pursue and prosecute physicians and laboratories considered to have violated the law. However, such enforcement activity is usually too little and too late.

Fourth, at a minimum, laboratories and pathology groups should conduct a rigorous legal review before entering into any type of arrangement which has even the appearance of linking financial reward to physician referrals. The risks from such arrangements are increasing, not decreasing. **TDR**

# INTELLIGENCE

**LATE & LATENT**  
 Items too late to print,  
 too early to report



It's a small news item, but sometimes such tidbits presage a bigger story. On Monday, September 26, 2005, **Quest Diagnostics Incorporated** filed a notice with the **Securities and Exchange Commission (SEC)** that it had received a subpoena from the New York Office of the U.S. **Department of Health and Human Services (HHS)**. The subpoena requested "various documents, including documents relating to Quest Diagnostics' relationship with health maintenance organizations, independent physician associations, group purchasing organizations and preferred provider organizations from 1995 to the present.

**MORE ON: Quest Subpoena**  
 Alert readers will recall that Quest Diagnostics and **Laboratory Corporation of America** received subpoenas earlier this summer from the U.S. Attorney in Newark, New Jersey. These subpoenas involved "business and financial records regarding capitation and risk-sharing arrangements with government and private

payers for the years 1993 through 1999." (See *TDR*, June 20, 2005.) Is it more than coincidence that federal offices on each side of the Hudson River are looking at certain laboratory contracting practices dating back to 1995?

## CROC BLOOD MAY YIELD POWERFUL NEW ANTIBIOTICS

Observing that crocodiles rarely suffer infections—*notwithstanding frequent violent injuries in microbe-laden environments*—a scientist at **McNeese State University** in Louisiana has collected samples of crocodile blood from Australia's tropical Northern Territory and is studying the creature's immune system. Studies in recent years showed that several antibodies in the reptile's blood kill penicillin-resistant bacteria, such as *Staphylococcus aureus*. Croc blood is also a more powerful killer of HIV than human serum. The reptile's immune system works by attaching to bacteria and tearing it apart, causing it to explode. McNeese State Biochemistry Professor Mark Merchant is working with crocodile blood samples to

isolate proteins that have antibiotic properties.

## ADD TO: Croc Blood

McNeese and fellow researchers expect that any resulting antibiotics would probably have to be synthesized for human consumption and could be delivered in tablet or ointment form. Merchant suggests that one topical application might be the treatment of diabetic ulcer wounds. Crocodile blood has also been of interest to scientists in the ongoing search for possible blood substitutes.

## "LEAN" LAB MANAGER WANTED

**Sacred Heart Medical Center** in Spokane, Washington recently posted a position for an Administrative Director of Laboratories with a unique qualification. It seeks a candidate with "Lean" experience, noting in the posting that "LEAN design techniques will be implemented as a part of the laboratory expansion project." The 623-bed tertiary care center is about to launch a major Lean makeover of its core laboratory.

*That's all the insider intelligence for this report.  
 Look for the next briefing on Monday, October 24, 2005.*



## ***UPCOMING...***

- How One Hospital Used Airline Pilots to Improve Physician-to-Physician Communication, Reducing Medical Errors and Malpractice Costs***
- Cervical Cancer Screening: Why Dollars Are Now Going to Find Untested Women.***
- Medicare Advantage: Will This New Program Disadvantage Hospital Lab Outreach Programs?***

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