

clients. The Centers for Medicare & Medicaid Services, or CMS, establishes procedures and continuously evaluates and implements changes to the reimbursement process.

We believe that most of our bad debt expense, which was 3.9% of our net revenues in 2006, is primarily the result of missing or incorrect billing information on requisitions received from healthcare providers and the failure of patients to pay the portion of the receivable that is their responsibility rather than credit related issues. In general, we perform the requested tests and report test results regardless of whether the billing information is incorrect or missing. We subsequently attempt to contact the healthcare provider or patient to obtain any missing information and rectify incorrect billing information. Missing or incorrect information on requisitions complicates and slows down the billing process, creates backlogs of unbilled requisitions, and generally increases the aging of accounts receivable and bad debt expense (see “Regulation of Reimbursement for Clinical Laboratory Services”). The increased use of electronic ordering reduces the incidence of missing or incorrect information. See “Recent Changes in Payer Relationships” for a discussion of our billing to UNH and its members.

## **Competition**

While there has been significant consolidation in the clinical laboratory testing industry in recent years, our industry remains fragmented and highly competitive. We primarily compete with three types of laboratory providers: hospital-affiliated laboratories, other commercial clinical laboratories and physician-office laboratories. We are the leading clinical laboratory testing provider in the United States, with net revenues of \$6.3 billion during 2006, and facilities in substantially all of the country’s major metropolitan areas. Our largest competitor is Laboratory Corporation of America Holdings, Inc. In addition, we compete with many smaller regional and local commercial clinical laboratories, specialized esoteric labs, as well as laboratories owned by physicians and hospitals (see “Payers and Customers”).

We believe that healthcare providers consider a number of factors when selecting a laboratory, including:

- service capability and quality;
- accuracy, timeliness and consistency in reporting test results;
- number and type of tests performed by the laboratory;
- number, convenience and geographic coverage of patient service centers;
- reputation in the medical community; and
- pricing.

We believe that we are an effective competitor in each of these areas.

We believe that large commercial clinical laboratories may be able to increase their share of the overall clinical laboratory testing market due to their large service networks and lower cost structures. These advantages should enable larger clinical laboratories to more effectively serve large customers and members of large healthcare plans. In addition, we believe that consolidation in the clinical laboratory testing industry will continue. However, a majority of the clinical laboratory testing is likely to continue to be performed by hospitals, which generally have affiliations with community physicians that refer testing to us (see “Payers and Customers – Hospitals”). As a result of these affiliations, we compete against hospital-affiliated laboratories primarily on the basis of service capability and quality as well as other non-pricing factors. Our failure to provide service superior to hospital-affiliated laboratories and other laboratories could have a material adverse effect on our net revenues and profitability.

The diagnostic testing industry is faced with changing technology and new product introductions. Advances in technology may lead to the development of more cost-effective tests that can be performed outside of a commercial clinical laboratory such as (1) near patient tests that can be performed by physicians in their offices; (2) esoteric tests that can be performed by hospitals in their own laboratories; and (3) home testing that can be carried out without requiring the services of clinical laboratories. Development of such technology and its use by our customers and patients would reduce the demand for our laboratory testing services and negatively impact our net revenues (see “Regulation of Clinical Laboratory Operations”). However, as a result of our acquisition of HemoCue, Focus Diagnostics and Enterix, we believe that we are well positioned to service this market for physicians and hospitals. We also believe that our overall near patient strategy will strengthen our relationship with our customers by enabling us to offer more solutions that improve their effectiveness and the care of their patients by enabling faster diagnosis and treatment. See “Recent Acquisitions”.