

near the patient will be available for electronic medical records and will display in similar format to tests performed in our centralized laboratories. This will differentiate our near patient testing products from other products that are not integrated into our customers' electronic records. Since July 2006, we have made several acquisitions that enable us to serve this near patient testing market, including HemoCue, Focus Diagnostics and Enterix. See "Recent Acquisitions". We believe that these acquisitions and 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. We will consider additional acquisitions or exclusive licenses of selective products to complement the products and services we provide.

- *Acquisitions and International Expansion:* The clinical laboratory industry in the United States remains fragmented. We expect to continue to selectively evaluate potential acquisitions of domestic clinical laboratories that can be integrated into our existing laboratories, thereby increasing access for patients and enabling us to reduce costs and improve efficiencies. While over the long term we believe positive industry factors in the U.S. diagnostic testing industry and the differentiated services we offer to our customers will enable us to grow organically, we see a number of opportunities to grow beyond our current principal business of operating diagnostic testing laboratories in the United States. We are actively exploring opportunities, including acquisitions, in the area of near patient testing to augment our laboratory testing business. Given that physicians and hospitals are primary sources for both near patient testing and laboratory performed tests, we believe providing both services will strengthen our relationships with customers and accelerate our growth.

Additionally, we see opportunities to bring our experience and expertise in diagnostic testing to international markets, particularly developing countries where the testing markets are highly fragmented and less mature. In addition, expansion into near patient testing and international markets will diversify our revenue base, and add businesses which are growing faster and are more profitable than our principal business of U.S. based clinical laboratory testing.

*People* enable us to realize our mission. In this regard, an important challenge is to prepare our workforce for the future. Our people strategy is built on concepts of stringent employee selection, effective engagement and ongoing development resulting in a staff of highly qualified and motivated employees who are committed to our goals. In addition, we are committed to improving the health of our employees and reducing healthcare costs for them and our Company. Through our HealthyQuest initiative, we provide employees with the opportunity to lose weight, quit smoking and generally pursue healthier lifestyles. Quest Diagnostics is recognized as a "best place to work" in numerous locales as a consequence of our workplace initiatives that reflect our belief that people are our most important asset. We take diversity seriously, believing that our organization should reasonably reflect the communities that we serve. We strive to make all of our employees effective ambassadors of our Company.

## **Recent Acquisitions**

On January 31, 2007, we acquired POCT Holding AB ("HemoCue"), a company headquartered in Angelholm, Sweden, that specializes in near patient testing, in an all-cash transaction valued at approximately \$420 million, including \$123 million of assumed debt of HemoCue. HemoCue, which has annualized revenues of approximately \$90 million, is the leading global provider in near patient testing for hemoglobin, with a growing share in the near patient markets for professional glucose and microalbumin testing. HemoCue's handheld systems are used in physician's offices, blood banks, hospitals, diabetes clinics and public health clinics. In developing countries these systems are used as the primary means to screen for anemia. The measurement of hemoglobin is important for patients being treated by transfusion, or undergoing dialysis or chemotherapy, where instant test results can lead to immediate treatment decisions. Approximately 50% of HemoCue's products are sold outside the United States. HemoCue has a strong product development pipeline, based on its pioneering use of its patented microfluidic systems, and is currently developing new tests, including one to determine white blood cell counts. This test will help physicians quickly determine the presence of an infection and, consequently, the need for antibiotic treatment, potentially reducing the overuse of antibiotics, an ongoing public health concern. In addition, we intend to make HemoCue's near patient handheld systems compatible with our Care360 portal, which enables doctors to store, access and share patient information. We financed the purchase price through a \$450 million one-year term loan.

In September 2006 we acquired Enterix, Inc. ("Enterix"), an Australia-based company, in an all-cash transaction valued at approximately \$44 million. Enterix manufactures the InSure™ fecal immunochemical test for screening for colorectal cancer and also performs the InSure™ test for patients. Prior to the acquisition, we

were the exclusive clinical laboratory offering the InSure™ test in the United States. During 2007, we intend to release a version of the test that can be performed by physicians in their offices.

On July 3, 2006, we acquired Focus Diagnostics Inc. (“Focus Diagnostics”) in an all-cash transaction valued at \$208 million, including approximately \$3 million of assumed debt. Focus Diagnostics is a leading provider of infectious and immunologic disease testing and has established a reputation for being first to introduce new assays to the market, including diagnostic tests for Lyme disease, West Nile Virus and SARS. In addition, Focus Diagnostics develops, manufactures and markets diagnostic products, such as HerpeSelect® ELISA tests that detect patient antibodies to specific types of Herpes Simplex Virus, which can be performed on a variety of instrument platforms. Subject to clearance by the Food and Drug Administration (“FDA”), we plan to introduce within the next year a near patient testing device that will allow physician office laboratories to rapidly detect antibodies against Herpes Simplex Virus type 2. Focus Diagnostics offers its reference testing services and sells its diagnostic products to large academic medical centers, hospitals and commercial laboratories. Focus Diagnostics’ facility is located in Cypress, California. Approximately 27% of Focus Diagnostics’ products are sold outside the United States.

We believe that the acquisition of HemoCue, Focus Diagnostics and Enterix support our growth strategy by establishing a platform to serve the near patient testing market. We expect to use HemoCue’s distribution network for sales of our complementary products, including Enterix’s near patient test for colorectal cancer screening, and Focus Diagnostics’ near patient product for Herpes Simplex Virus type 2 antibodies, as well as other diagnostic products that we develop. We also plan to investigate the potential applications of research conducted at Focus Diagnostics to HemoCue’s device platform. In addition to adding new product development capabilities, the acquisition of Focus Diagnostics further solidifies our leading position in providing esoteric testing for hospitals and commercial laboratories by adding Focus Diagnostics’ infectious and immunologic disease testing services to our menu.

On November 1, 2005, we acquired LabOne, Inc., (“LabOne”), in a transaction valued at approximately \$947 million, including approximately \$138 million of assumed debt of LabOne. LabOne provides health screening and risk assessment services to life insurance companies, as well as clinical diagnostic testing services to healthcare providers and drugs-of-abuse testing to employers. LabOne operates regional laboratories in Lenexa, Kansas, and Cincinnati, Ohio, as well as a state-of-the-art call center in Lee’s Summit, Missouri, and provides paramedical examination services throughout the United States and Canada to serve the life insurance industry. The acquisition of LabOne supports our growth strategy in a number of ways, including: solidifying our leadership position in diagnostic testing by expanding access for physicians and patients and giving us added presence in several geographic areas; strengthening our drugs-of-abuse testing business and establishing us as the leader in a new testing-related business, providing health screening and risk assessment services to the life insurance industry.

### **Recent Changes in Payer Relationships**

On October 3, 2006, we announced that we would not be a national contracted provider of laboratory services to United Healthcare Group, Inc., (“UNH”), beginning January 1, 2007. After negotiating with UNH and offering to substantially reduce their total costs for laboratory services, UNH demanded that we execute an agreement that would have significantly reduced fees from what we had offered, and would have given UNH the right to unilaterally dictate certain key terms over a period of up to eight years. We determined that in the long term, signing such an agreement would not be in the best interest of our Company and our shareholders.

UNH accounted for approximately 7% of our net revenues in 2006, with some of our regional laboratories having concentrations as high as 15% to 20%. As one of many contracted providers, we estimate that we served approximately half of UNH’s members or approximately three times as many as our single largest competitor. We believe that this was because physicians and patients preferred using us due to quality and convenience. While we expect to continue to service UNH’s members in certain limited markets as a contracted provider and in other markets as a non-contracted provider, UNH has threatened physicians with penalties if they continue to send laboratory testing to a non-contracted provider as of March 1, 2007. We believe UNH’s actions are unprecedented and inappropriate, because they effectively eliminate the choice to use an out-of-network provider which is embedded in many of the products UNH sells, and which employers and patients paid for. In addition, UNH has been aggressively communicating to its members that they may be faced with higher co-payments and deductibles if they use an out-of-network laboratory. While we retained virtually all of our UNH business through December 31, 2006, we estimate that by February 16, 2007, about 60% of our direct UNH business has moved to various contracted providers. We currently expect that the vast majority of the work we perform for UNH members will move to contracted providers before the end of 2007. However, it is possible that if patients and