

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

physicians are sufficiently dissatisfied with the services they receive from providers UNH is requiring them to use, we may regain some of the lost business.

In most cases when we perform testing for UNH members as a non-contracted provider we are entitled to reimbursement and UNH is required to pay for our services, often at rates in excess of what we were previously reimbursed. However, we expect UNH may challenge our rights to reimbursement in certain cases, leading to disputes which will take time to resolve, and could result in a temporary increase in days sales outstanding. UNH may also decide to remit payment to patients for the services we provide them as a non-contracted provider, requiring us to pursue the patient for collection. Pursuing collections from patients generally requires more effort and is more costly than collecting from a healthcare insurer and carries greater collection risk. Therefore, if we are required to collect from patients rather than UNH, we could experience higher collection costs and bad debt on the work we perform as a non-contracted provider. We plan to aggressively assert and defend our rights to appropriate reimbursement, and challenge certain of UNH's actions on a number of fronts. In addition, we are educating patients, their physicians and employers that there are important differences between laboratory testing providers, and that their right to choose their testing provider should not be eliminated by inappropriate methods.

Our current expectation is that no longer being a contracted provider to UHN, and becoming a non-contracted provider to Horizon Blue Cross Blue Shield of New Jersey (which accounted for approximately 1% of our net revenues in 2006), will reduce our revenue growth in 2007 by between 7% and 10%, most of that resulting from the direct loss of previously contracted work, and some of it associated with the loss of other work from physicians who choose to consolidate their testing with a single laboratory. Given that we expect a decrease in volume levels in 2007 due to these contract changes, we plan to adjust our cost structure to match the new volume levels. However, due to the fact that a large portion of our costs, approximately 40% or more, are fixed, we do not expect our cost reduction actions will fully mitigate the profit impact of the anticipated volume decline during 2007. Our plans also include examining our structural, or fixed costs, to determine what reductions can be made. The extent to which we will need to reduce structural costs, which in part will be driven by how quickly we replace lost business, will determine how long it will take to complete all of our cost actions. As we do so, top priorities will be maintaining the differentiated level of service we provide to our patients and physicians, and remaining positioned to capitalize on growth opportunities.

Our Services

For 2006, our clinical laboratory testing business accounted for approximately 92% of our net revenues, with the balance derived from risk assessment services, clinical trials testing, healthcare information technology services and diagnostic products. Substantially all of our services are provided within the United States. See Note 16 to the Consolidated Financial Statements. Laboratory testing includes routine testing and gene-based and esoteric testing, which generated approximately 76% and 16%, respectively, of our net revenues. Risk assessment services generated approximately 5% of our net revenues and clinical trials testing generated approximately 3% of our net revenues. We derive approximately 2% of our net revenues from foreign operations.

Routine Testing

Routine tests measure various important bodily health parameters such as the functions of the kidney, heart, liver, thyroid and other organs. Commonly ordered tests include:

- blood cholesterol level;
- blood chemistries;
- complete blood cell counts;
- Pap tests;
- urinalyses;
- pregnancy and other prenatal tests;
- alcohol and other substance-abuse tests; and
- asthma and allergy tests such as the ImmunoCap® test.

We perform routine testing through our network of major laboratories, rapid response laboratories and patient service centers. We also perform routine testing at the hospital laboratories we manage. Major laboratories offer a full line of routine clinical tests. Rapid response laboratories are smaller facilities where we can quickly perform an abbreviated menu of routine tests for customers that require rapid turnaround times. Patient service centers are