QUEST DIAGNOSTICS INC
Form 10-K
February 17, 2009

2008 Annual Report
on Form 10 K

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of
the Securities Exchange Act of 1934
For the Fiscal Year Ended December 31, 2008
Commission File Number 001-12215

Quest Diagnostics Incorporated

3 Giralda Farms
Madison, New Jersey 07940
(973) 520-2700

Delaware
(State of Incorporation)

16-1387862
(I.R.S. Employer Identification Number)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	*Name of Each Exchange on Which Registered*
Common Stock, $.01 par value per share	New York Stock Exchange

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Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.
Yes o No x

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer (do not check if a smaller reporting company) o Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No x

As of June 30, 2008, the aggregate market value of the approximately 158 million shares of voting and non-voting common equity held by non-affiliates of the registrant was approximately $7.7 billion, based on the closing price on such date of the registrant s Common Stock on the New York Stock Exchange.

As of January 30, 2009, there were outstanding 190,574,834 shares of Common Stock, $.01 par value per share.

Documents Incorporated by Reference

Document	Part of Form 10-K into which incorporated
Portions of the registrant s Proxy Statement to be filed by April 28, 2009	Part III

Such Proxy Statement, except for the portions thereof which have been specifically incorporated by reference, shall not be deemed filed as part of this report on Form 10-K.

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Item 1. Business

Quest Diagnostics Incorporated is the world s leading provider of diagnostic testing, information and services. We provide insights that enable patients, physicians and others to make decisions to improve health.

Quest Diagnostics was incorporated in Delaware in 1990; its predecessor companies date back to 1967. We conduct business through our headquarters in Madison, New Jersey, and our laboratories, patient service centers, offices and other facilities around the United States and in selected locations outside the United States. Unless the context otherwise requires, the terms Quest Diagnostics, the Company, we and our mea Quest Diagnostics Incorporated and its consolidated subsidiaries.

During 2008, we generated net revenues of $7.2 billion and processed approximately 150 million test requisitions. Additional financial information concerning Quest Diagnostics, including our consolidated subsidiaries, for each of the years ended December 31, 2008, December 31, 2007 and December 31, 2006 is included in the consolidated financial statements and notes thereto in Financial Statements and Supplementary Data in Part II, Item 8.

OUR STRATEGY AND STRENGTHS

Our mission is to be the undisputed world leader in diagnostic testing, information and services. Our vision is that we are dedicated people improving the health of patients through unsurpassed diagnostic insights and innovation. We focus on patients, growth and people to help achieve our goals.

We offer high value diagnostic testing services and products attractive to patients, physicians, payers, and others and have become the provider of choice in key areas of the diagnostic testing market. We believe that successful execution of our strategy will drive continued growth of our business. Additionally, we believe that, over the long term, we will be able to grow at a rate above the U.S. clinical laboratory industry growth rate, to expand margins and to increase international revenues to 10% of consolidated revenues. We plan to do this by gaining more customers, selling more services and products to existing customers and by continuously improving the efficiency of our operations. The elements of our growth strategy are described below.

Deliver a superior patient experience. The patient is at the center of everything we do. Increasingly, patients have a choice when it comes to selecting a healthcare provider and we strive to give patients compelling reasons to put their trust in us. We have made significant investments in training our employees to provide a superior patient experience. We believe that this will drive patient and physician loyalty. Additionally, we have deployed automated patient appointment scheduling for our patient service centers. This enables patients to schedule appointments at times that are convenient for them while essentially eliminating their waiting time. We believe that we are the only national clinical test provider that offers this service in almost all of its patient service centers. We also collaborated with Google to launch Google Health , which allows patients to share, save, organize and manage online their medical records and personal health information, including diagnostics laboratory data.

Continuously drive Six Sigma quality. We strive to provide the highest quality in all that we do, including: phlebotomy and specimen transport services; analytical testing processes in our laboratories; accurate and timely lab reports; and accurate and timely billing. We use Six Sigma and Lean processes to continuously reduce defects, enhance quality and further increase the efficiency of our operations. Six Sigma is a management approach that utilizes a thorough understanding of customer needs and requirements, root cause analysis, process improvements and rigorous tracking and measuring to enhance quality. Lean is a management approach that seeks to streamline processes and eliminate waste. We also use Six Sigma and Lean principles to help standardize operations and processes across our Company and identify and adopt company best practices. We believe our focus on continuously driving Six Sigma quality in all aspects of our business results in superior service to our customers and drives customer loyalty.

Leverage our unparalleled assets and capabilities. We are the world leader in the clinical testing business and the leading cancer diagnostic testing provider. We have the most extensive clinical testing network in the United States, offering national access to testing services. We operate a nationwide network of over 2,000 of our own patient service centers where we collect patient specimens, and laboratories in most major metropolitan areas. We provide anatomic pathology services, including inpatient anatomic pathology and medical director services at hospitals, throughout the country. We have a leading medical and scientific staff of approximately 900 M.D.s and Ph.D.s, primarily located in the United States. We serve approximately half of the physicians and half of the hospitals in the United States. We also operate approximately 75 locations in the United States and Canada where we coordinate the provision of paramedical examinations related to life insurance applications. We offer the broadest test menu, with more than 3,000 tests, and are the leading provider in the United States of gene-based and other esoteric testing. We have strong logistics capabilities, such as approximately 3,500 courier vehicles and 25 airplanes that make approximately 90,000 stops daily. We believe that customers and payers

prefer providers that offer a comprehensive range of tests and services and the most convenient access to those services and that, by offering such services, we will be able to profitably enhance our market position.

Continue to lead in medical innovation and information technology solutions. We are a leading innovator in the clinical testing market with unmatched medical and technical expertise. We have the most comprehensive test menu and leading medical and scientific experts available for consultation. Over the past several years, we have expanded our business in more complex and faster-growing testing areas, including gene-based and esoteric testing, anatomic pathology services and point-of-care testing, reducing the percentage of our revenues from routine testing services. We remain a leading innovator in the clinical testing industry by continuing to introduce new tests, technology and services, including in the evolving area of personalized and targeted medicine. As an industry leader with the largest and broadest U.S. network and expanding presence outside the United States, we believe we are the channel of choice for developers of new tests to introduce their products to the marketplace. Through our relationships with the academic medical community and pharmaceutical and biotechnology firms, we believe that we are a leader in bringing technical innovation to the market. For example, in 2008, we expanded our growing menu of plasma-based Leumeta tests to 22.

We empower healthcare organizations and clinicians with information technology solutions that can improve patient care and medical practice. We develop products, such as ChartMaxx®, and the Care360 Physician Portal, and a clinical portal that are designed to support the creation and management of electronic patient records, by bringing together, in one patient-centric view, information that includes physician s records and laboratory and hospital data. Our Care360 products, which can be accessed by more than 140,000 physicians, enable physicians to order diagnostic tests and review test results online. In addition, the Care360 Physician Portal enables physicians to electronically prescribe medication, view clinical and administrative information from various sources, file certain documents into a patient-centric health record maintained in our repository and share confidential information with medical colleagues. We believe that these products enhance the value we provide to our customers and result in increased customer loyalty.

Expand our geographic reach. In addition to growth opportunities in the United States, we see opportunities to expand our presence in Ireland and Mexico and to bring our experience and expertise in diagnostic testing to other international markets, particularly to developing countries where the testing markets are highly fragmented and less mature. During 2008, we began offering services and products in the growing market in India. Our product offering in India includes clinical testing for life insurance companies, clinical trials testing for global pharmaceutical companies, advanced esoteric testing for hospitals, physicians and patients, point-of-care products and wellness testing.

Expand our diagnostic scope. Technology advances are enabling testing to move closer to the patient and are becoming increasingly available and reliable. This enables more timely and effective decisions, with the opportunity to improve patient care and reduce medical costs. Since July 2006, we have acquired three businesses that offer point-of-care, or near patient, testing: HemoCue, Focus Diagnostics and Enterix. We intend to expand their product menus, develop novel technology platforms and systems to meet the needs of our clients and pursue potential additional acquisitions to supplement our offering. Results of their tests can be entered into our Care360 system, enabling the integration of tests performed in a near patient setting with those performed in our laboratories. We are well positioned to offer choice and integrated solutions to physicians, hospitals, clinics and retail customers for the testing methods that are most appropriate for each patient and practice.

In support of our strategy, in recent years we have undertaken several acquisitions. These acquisitions enable us to expand our capabilities, further leverage our assets and differentiate our Company from our competition, diversify our revenues and accelerate our growth. We expect to continue to selectively evaluate acquisitions in the United States and in select international markets.

BUSINESS OPERATIONS

Quest Diagnostics is the world s leading provider of diagnostic testing, information and services, providing insights that enable patients, physicians and others to make decisions to improve health. We offer U.S. patients and physicians the broadest access to diagnostic testing services through our nationwide network of laboratories and Company-owned patient service centers. We provide interpretive consultation through the largest medical and scientific staff in the industry, with approximately 900 M.D.s and Ph.D.s, primarily located in the United States. We are the leading provider of clinical testing, including gene-based and other esoteric testing, anatomic pathology services, including dermatopathology and testing for drugs-of-abuse, and the leading provider of risk assessment services for the life insurance industry. We are also a leading provider of testing for clinical trials. Our diagnostics products business manufactures and markets diagnostic test kits and specialized point-of-care testing. We empower healthcare organizations and clinicians with robust information technology solutions. Our activities are described below.

Patients are at the center of everything that we do. We are leveraging our diagnostic testing capabilities and our assets to serve multiple customer bases. In 2008, our clinical testing business accounted for greater than 90% of our net revenues, with the balance derived from insurer services, clinical trials testing, diagnostic products and healthcare information technology. Most of our services are provided in the United States. Clinical testing includes routine testing, anatomic pathology, gene-based and esoteric testing, and drugs-of-abuse testing, which generated approximately 52%, 16%, 20% and 3%, respectively, of our 2008 net revenues. Risk assessment services for the life insurance industry, clinical trials testing, diagnostic products and healthcare information technology combined generated approximately 9% of our 2008 net revenues. In 2008, we derived approximately 3% of our net revenues from foreign operations and held approximately 7% of our long-lived assets outside the United States.

Clinical Testing. We are the world s largest commercial clinical testing company. We offer customers the broadest access to the most extensive test menu of clinical and anatomic pathology tests in the United States. Clinical testing is an essential element in the delivery of healthcare services. Physicians use clinical tests to assist in the detection, diagnosis, evaluation, monitoring and treatment of diseases and other medical conditions. Clinical testing is generally categorized as clinical laboratory testing and anatomic pathology services. Clinical laboratory testing generally is performed on blood and body fluids, such as urine. Anatomic pathology services are performed on tissues, such as biopsies, and other samples, such as human cells. Clinical tests which can be performed by most clinical laboratories are considered routine. Esoteric tests are clinical tests that are not routine, require highly skilled personnel and generally require more sophisticated equipment. Esoteric tests, including gene-based tests, generally are performed in several of our laboratories. As testing methods become more complex, we believe that providing sound medical and scientific consultation regarding tests and test results will help spur the adoption of new tests, improve patient outcomes and enhance customer satisfaction. To this end, we have in-house medical directors, scientific directors and genetic counselors available for consultation with our customers.

Routine clinical testing. We are the leading provider of routine clinical testing, including testing for drugs-of-abuse. We perform routine testing through our network of major laboratories and rapid response laboratories. We also perform routine testing at the hospital laboratories we manage. Rapid response laboratories are smaller facilities where we can quickly perform an abbreviated menu of routine tests for customers that require rapid turnaround times. We also perform routine testing at hospital laboratories that we manage. We operate 24 hours a day, 365 days a year, performing and reporting most routine tests within 24 hours. The majority of test results are delivered electronically.

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 chemistries, including cholesterol levels;
- complete blood cell counts;
- urinalyses;
- pregnancy and other prenatal tests;
- routine microbiology testing;
- alcohol and other substance-abuse tests; and
- allergy tests such as the ImmunoCap® test.

Anatomic Pathology. We are the leading provider of cancer diagnostics, including anatomic pathology services in the United States. Anatomic pathology involves the diagnosis of cancer and other diseases and medical conditions through examination of tissue and cell samples taken from patients. We provide anatomic pathology and other cancer diagnostics testing, including inpatient anatomic pathology and medical director services at hospitals, throughout the country, including through our major laboratories. We have a substantial presence in select areas and strong relationships with ordering physicians.

We significantly strengthened our anatomic pathology services offering through our May 2007 acquisition of AmeriPath Group Holdings, Inc. (AmeriPath). We provide a full-range of cancer diagnostic services to all specialties including: dermatopathology, gastroenterology, hematology, urology and oncology. We have approximately 700 board-certified pathologists, including luminaries in their field, with a passion for and dedication to serving patients with the highest quality service.

We have a strong history of leadership and innovation in cancer diagnostics. We introduced the Leumeta family of tests for leukemia and lymphoma. These proprietary plasma-based molecular tests may some day eliminate the need for painful bone marrow biopsies. We offer Pap testing using liquid-based technology in addition to conventional Pap testing and provide physicians the option of computer assisted Pap screening. We were one of the industry leaders

educating physicians about molecular testing for human papilloma virus (HPV), the leading cause of cervical cancer. During 2008, the National Cancer Screening Service of the Republic of Ireland selected the Company to provide cervical cancer screening testing for women age 25 to 60 participating in Ireland s first nationwide cytology-screening program.

Gene-Based and Other Esoteric Testing. Gene-based and other esoteric tests increasingly are ordered by physicians to assist in the diagnostic process, to establish a prognosis and to choose or monitor a therapeutic regimen. Esoteric tests include procedures in the areas of molecular diagnostics, protein chemistry, cellular immunology and advanced microbiology. Commonly ordered esoteric tests include viral and bacterial detection tests, drug therapy monitoring tests, autoimmune panels and complex cancer evaluations. Esoteric tests typically require professional hands-on attention from highly-skilled technical personnel, generally require more sophisticated technology, equipment or materials and may be performed less frequently than routine tests. Consequently, esoteric tests are generally reimbursed at higher levels than routine tests. It is not practical, from a cost-effectiveness or infrastructure perspective, for most hospitals, independent laboratories or physician office laboratories to develop and perform a broad menu of esoteric tests, or to perform low-volume esoteric testing in-house. Such tests generally are outsourced to an esoteric clinical testing laboratory, such as our Nichols Institute or Focus Diagnostics, which specializes in performing these complex tests.

We are the leading provider in the United States of gene-based and other esoteric testing, with net revenues of over $1.4 billion, or 20% of consolidated net revenues, in 2008. We conduct complex and specialized testing, including molecular diagnostics, in our two world renowned Nichols Institute laboratory facilities (one on each U.S. coast), and in a number of other locations.

Our esoteric laboratories provide reference testing services to physicians, large academic medical centers, hospitals and other commercial laboratories. Our esoteric testing laboratories perform hundreds of complex tests that are not routinely performed by our regional laboratories, including but not limited to the following fields:

endocrinology and metabolism (the study of glands, their hormone secretions and their effects on body growth and metabolism);

genetics (the study of chromosomes, genes and their protein products and effects);

hematology (the study of blood and bone marrow cells) and coagulation (the process of blood clotting);

immunogenetics and human leukocyte antigens (HLA) (solid organ and bone marrow transplantation; eligibility for vaccines; selection of pharmacotherapeutic agents and immunotherapy);

immunology (the study of the immune system, including antibodies, cytokines, immune system cells and their effect, receptor systems and autoimmune diseases);

microbiology and infectious diseases (the study of microscopic forms of life, including parasites, bacteria, viruses, fungi and other infectious agents);

oncology (the study of abnormal cell growth, including benign tumors and cancer);

serology (a science dealing with body fluids and their analysis, including antibodies, proteins and other characteristics); and

toxicology (the study of chemicals and drugs and their adverse effects on the body).

We believe that offering a full range of gene-based and other esoteric tests strengthens our market offering and market position and enhances our reputation as the nation s leading test provider.

Scientific Innovation. We are a leading innovator in the clinical testing industry, with the ability to develop technologies from the earliest discovery stage to a commercially validated clinical test. We develop tests at our laboratories, such as Quest Diagnostics Nichols Institute and Focus Diagnostics, and develop innovative techniques in anatomic pathology. We are a leader in transferring technical innovations to the market through our relationships with technology developers, including the academic community and pharmaceutical and biotechnology firms, as well as through collaborations with emerging medical technology companies that develop and commercialize novel diagnostics, pharmaceutical and device technologies. We search for new opportunities and continue to build a robust pipeline of new tests in screening, diagnosis, prognosis and treatment choice, which assists in early detection of diseases and may reduce healthcare costs. Through our strengths in assay development, distribution and commercialization, we believe that we are the best partner for developers of new technologies and tests to introduce their products to the marketplace.

We focus our resources on key disease states and technologies to help doctors care for their patients through better screening, monitoring, diagnosis, prognosis and treatment choices. We also look for tests that are less invasive than currently available options. With these priorities in mind, in 2008, we introduced a number of new tests. A representative sampling of recent new tests is set forth below.

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Oncology.

- We expanded to 22 our growing menu of plasma-based Leumeta tests. These tests are useful in determining many different types of hematological disorders, and in particular, use qualitative findings to assist in the diagnosis of certain hematological disorders in patients who lack the *JAK2* mutation. Plasma-based assays are an effective and less invasive way of diagnosing and monitoring leukemia and lymphoma patients and allows for more frequent disease progression monitoring, compared to other laboratory diagnostic methods that require patients to undergo painful procedures, such as bone marrow biopsies.

- We introduced *KRAS* Mutation Analysis, a molecular test that helps to determine if patients with metastatic colorectal or lung cancer are eligible for treatment with EGFR-targeted therapy.

- We introduced HE4, a new serum-based test exclusively licensed from Fujirebio. HE4 is the first test in the last 20 years to receive clearance from the U.S. Food and Drug Administration (FDA) for monitoring woman with ovarian cancer. This test provides valuable information in determining patient prognosis and is selected in certain instances by physicians who traditionally order the CA125 test for monitoring.

- We introduced InScape Virtual Pathology which is a novel Immunohistochemistry (IHC) that allows pathologists to access their cases through a secured HIPAA compliant website. This supports a pathologist s ability to remotely review stained slides and provide information back to treating physicians more quickly and reduce the anxious waiting time of patients.

- We licensed the Septin 9 biomarker. Methylation of the Septin 9 gene is a marker in blood plasma of colorectal cancer patients. We plan to develop plasma-based colorectal cancer screening tests using the Septin 9 marker to act as a supplement to conventional methods of colorectal cancer screening, including colonoscopy and fecal occult blood tests. Too often, patients fail to undergo a colonoscopy or conduct other types of colorectal cancer screenings because they find these methods invasive, unpleasant or costly. A blood test for detecting colorectal cancer, once developed, will be a convenient option that complements other screening methods.

- We also licensed and are developing additional oncology applications for our ClariSure CGH (Comparative Genomic Hybridization) Assay.

Urology.

- We acquired exclusive rights to and launched the UroRisk Diagnostics Profile and the StoneRisk Diagnostics Profile. These tests are considered to be the gold standard for kidney stone risk assessment and monitoring of recurrence and help determine lifestyle changes needed to avoid further stone development.

Infectious Disease.

- We continued to expand our menu of tests focused on esoteric infectious diseases, drawing on our expertise and strength in this field. Our Focus Diagnostics subsidiary was the first CLIA-approved service laboratory in the United States to develop and introduce a test for detecting the mosquito-borne Chikungunya virus. Commercial availability of this molecular polymerase chain reaction (PCR) test enables physicians to test patients who may have contracted the virus while traveling to endemic areas.

- We also introduced a PCR-based test which detects virtually all known enterovirus strains, along with multiple parecho virus strains that cause infections that can be especially severe in infants and young children.

Genetics and Personalized Medicine. Increasingly, tests will be introduced that determine a patient s genotype or gene expression profile associated with a particular disease. These tests can help physicians to determine a patient s susceptibility to disease or to tailor medical care to an individual s needs such as determining if a medication might be more or less effective for a particular person, or which of several medications might work better, and tailoring the right dosage once the proper medicine is prescribed. A few examples are set forth below:

- Carbamazepine is a common anti-seizure and pain medication, which has the potential for a severe and sometimes fatal dermatologic reaction. This risk is 10-fold higher in Asians. We introduced the HLA (Human Leukocyte Antigen) test to screen Asian patients, thus helping physicians identify which patients should not be given carbamazepine.

- The leading cause of vision loss in older individuals is age-related macular degeneration, which typically starts showing symptoms, such as blurring in one s central vision, in the fifth decade of life. We introduced the Macular Degeneration Mutation Analysis that helps determine one s risk of developing age-related macular degeneration.

- Aspirin therapy is often prescribed to prevent atherothrombosis. However, sometimes aspirin does not work, and there may be issues with patient compliance and the correct dosage. We introduced the Corgenix AspirinWorks® test, a urine test that helps identify patients that do not respond to aspirin therapy.

In addition, we recently acquired additional biomarker capabilities to advance our efforts to develop companion diagnostics for new therapies that will enable personalized patient treatment.

Clinical Trials Testing. We believe that we are the second largest provider of central laboratory testing performed in connection with clinical research trials on new drugs and vaccines. Clinical research trials are required by the FDA and other international regulatory authorities to assess the safety and efficacy of new drugs and vaccines. We see opportunities to develop pharmacogenetic tests to help speed drug approval processes for our clinical trials customers and, capitalizing on the trend to personalized medicine, better focus patient therapy based on patient genetic markers.

We have clinical trials testing centers in the United States, the United Kingdom and India, and we provide clinical trials testing in Australia, China and Singapore through affiliated laboratories. While we serve most of the major pharmaceutical companies, approximately 40% of our net revenues from clinical trials testing in 2008 represented testing for GlaxoSmithKline plc (GSK). We are the primary provider of central laboratory testing to support GSK s clinical trials testing requirements worldwide.

Life Insurer Services. We are the largest provider of risk assessment services to the life insurance industry in the United States and Canada. We also provide risk assessment services for insurance companies doing business in many countries outside the United States. In 2008, we began providing risk assessment services in India.

Our risk assessment services comprise underwriting support services to the life insurance industry including teleunderwriting, specimen collection and paramedical examinations, clinical testing, medical record retrieval, case management, motor vehicle reports, telephone inspections, prescription histories and credit checks. The clinical tests that we perform and data we gather are designed specifically to assist insurance companies in objectively evaluating the mortality and morbidity risks posed by policy applicants. The majority of the testing is performed on specimens of life insurance applicants, but also includes specimens of applicants for other types of insurance. Factors such as the number of applications for fully-underwritten life insurance policies can affect the utilization of clinical testing and other services we provide to our insurance customers. Most of our specimen collections and paramedical examinations are performed at the applicant s home or workplace. We operate approximately 75 locations other than patient service centers in the United States and Canada where we provide paramedical examinations. We have been actively performing paramedical examinations in select patient service centers and during the first quarter of 2009, we plan to offer paramedical examinations through 500 of our patient service centers, bringing to approximately 575 the total number of sites where we provide these examinations. We also contract with third parties at over an additional 125 locations across the United States and Canada to coordinate providing these exams.

We seek to grow our insurance revenues by increasing our market share and by offering new and innovative clinical tests and other services. Our life insurance customers have been consolidating, which has resulted in increased individual customer purchasing power. We expect that this trend will continue. We charge our life insurance customers on a fee-for-service basis, typically under multi-year agreements.

Employer Services. We believe that we are the leading provider of clinical testing to employers for drugs-of-abuse. Our Drug Testing Index, which is an annual report of our aggregate drug testing results, is used nationally by employers, the federal government and the media to help identify and quantify drug abuse among the nation s workforce.

As healthcare costs have increased, so has the value of preventative care. Employers grappling with increased healthcare costs are considering wellness testing as a key tool to reduce their healthcare costs. We provide wellness testing to employers to enable their employees to take an active role in improving their health and empower employers with aggregated health information. Our Blueprint for Wellness program offers employers actionable data to power their health improvement and cost containment programs. We are leveraging our patient service centers and paramedical network to deliver wellness screening nationwide. Additionally, in the fourth quarter of 2008, we began to offer Blueprint for Wellness directly to individuals through our partnership with Google Health .

Diagnostic Products, Including Point-of-care, or Near Patient, Testing. Technology advances are enabling testing to move closer to the patient and are becoming increasingly available and reliable. Over time, some testing that is now done in clinical laboratories will cease to be performed in clinical laboratories and will be performed closer to the

patient. We believe that our point-of-care testing strategy will strengthen our relationship with our customers by enabling us to offer more solutions that improve the effectiveness of our customers and the care of their patients by enabling faster diagnosis and treatment. We are well positioned to offer options and integrated solutions to physicians, hospitals and clinics for the testing methods that are most appropriate for each patient and practice.

We develop and manufacture products that enable healthcare professionals to make healthcare diagnoses, including products for point-of-care, or near patient, testing for the professional market. Since July 2006, we have acquired several companies, including Focus Diagnostics, Enterix, and HemoCue, that enhance our offerings and better enable us to serve these markets. We will consider additional acquisitions or licenses of selective products to complement the products and services we provide. The results of the InSure® Quik FIT™ point-of-care test and HemoCue hemoglobin, glucose, urine albumin and white blood cell tests, as well as tests performed by our laboratories, can be entered into our Care360 Physician Portal so that they all are available in one electronic medical record. We intend to offer additional data links in the future. This will differentiate our point-of-care test products from other products that are not integrated into an electronic repository.

Focus Diagnostics is a leading provider of infectious disease testing that has established a reputation for being first to introduce new tests to the market, including diagnostic tests for Lyme disease, West Nile Virus and SARS. 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. Focus received FDA 510(k) clearance to sell in the United States its new multiplexed Plexus™ product to detect type specific antibodies to herpes simplex virus. Focus has also submitted an application to the FDA for 510(k) clearance to allow U.S. sales of Plexus™ products for the detection of antibodies specific to Epstein-Barr virus. Both the Plexus™ products have received the CE mark and are available for purchase in European Union countries. Focus Diagnostics sells its diagnostic products to large academic medical centers, hospitals and commercial laboratories globally.

HemoCue, headquartered in Angelholm, Sweden, specializes in point-of-care testing. HemoCue is the leading global provider in point-of-care testing for hemoglobin, with a growing market share for glucose, microalbumin and white blood cell testing. The measurement of hemoglobin is important for blood donors and for patients being considered for transfusion therapy, or undergoing dialysis or chemotherapy, where instant test results can lead to immediate treatment decisions. The HemoCue 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. Approximately one-half of HemoCue products are sold outside the United States. We believe that HemoCue has a strong product development pipeline, based on its pioneering use of its patented microfluidic systems.

In October 2007, HemoCue received FDA 510(k) clearance for its White Blood Cell Analyzer, a whole-blood test performed on finger-stick samples that can assist physicians by providing a total white blood cell count (WBC). Changes in WBC may be indicative of infection, inflammation, bone marrow failure, autoimmune diseases and many other medical conditions. The WBC can be useful to physicians in helping to diagnose a patient s disease state and determine at the point of care what, if any, treatment may be appropriate for the patient in conjunction with other clinical signs and symptoms. WBC is a test routinely performed by most laboratories. In addition, Focus Diagnostics received FDA 510(k) clearance for its HerpeSelect® Express HSV-2, which is used for aiding in the diagnosis of herpes simplex type-2 virus, the primary cause of genital herpes. With 510(k) clearance for marketing, physicians who operate CLIA-certified moderately complex laboratories may now use these two products to quickly produce results in a single office visit. These two tests can help physicians quickly determine the possible presence of an infection and allow physicians to make more informed and immediate treatment decisions for their patients. We have applied for CLIA-waived status for these two products which, if granted, would permit physicians to use these products in a much larger segment of physician offices. In 2008, a CLIA waiver was granted for our urine albumin test.

Enterix, an Australia-based company, manufactures the InSure® fecal immunochemical test (FIT) for screening for colorectal cancer and has developed the InSure® Quik FIT test for processing by the physician in his or her office.

International. We have laboratory facilities in Mexico City, Mexico; San Juan, Puerto Rico; Gurgaon, India; and Heston, England. These laboratories support our clinical trials business and clinical testing in their local markets. In India, our laboratory also supports our risk assessment services and sales directly to employers and consumers. We also have sales representatives dedicated to offering our point-of-care test products in countries outside the United States. We see opportunities to bring our experience and expertise in diagnostic testing and point-of-care products to international markets, particularly developing countries where the testing markets are highly fragmented and less mature.

Healthcare Information Technology. We empower healthcare organizations and clinicians with information technology solutions that can improve patient care and medical practice. We develop differentiated products that are designed to support the creation and management of patient records, by bringing together, in one patient-centric view, information from various sources, including physician s records and laboratory and hospital data. We believe that these

products enhance the value we provide to our customers and result in increased customer loyalty by providing more convenient ordering and reporting of clinical tests and better access to patient-centric information.

We develop and integrate clinical connectivity and data management solutions for healthcare organizations, physicians and clinicians primarily through our Care360 suite of products and the ChartMaxx® electronic document management system for hospitals. The Care360 products, including our Care360 Physician Portal, enable physicians to order diagnostic tests and review test results from Quest Diagnostics online. In addition, the Care360 Physician Portal enables physicians to electronically prescribe medication, view clinical and administrative information in a patient-centric record maintained in our repository and share confidential information with medical colleagues in a HIPAA-compliant manner. Demand has been growing for our information technology solutions as physicians have expanded their usage of the Internet. By the end of 2008, approximately 140,000 physicians had access to Care360 products. Excluding our AmeriPath business, over 70% of our test orders and approximately 85% of our test results were being transmitted electronically. E-prescribing medications processed through Care360 in 2008 more than doubled compared to 2007. The annualized rate as we exited 2008 was 4.5 million. We believe that recent e-prescribing incentives promulgated by the Centers for Medicare and Medicaid Services (CMS) will foster increased demand for our information technology solutions.

Additionally, in 2007 we acquired the capabilities to deploy a health information exchange system comprised of proprietary technologies that enable healthcare providers to access and manage a range of patient data from multiple sources at the point-of-care. These capabilities will enable us to provide solutions to the many health information exchanges that are being developed.

In 2008, we collaborated with Google to launch Google Health . Google Health enables patients and physicians to share diagnostic laboratory data online, and allows users to save, organize and manage their medical records and personal health information online. Using our Care360 connectivity products, physicians can securely provide diagnostic data with a brief explanation of test results to a patient s Google Health account.

THE UNITED STATES CLINICAL TESTING MARKET

Most clinical tests are performed by one of three types of laboratories: commercial clinical laboratories; hospital-affiliated laboratories; and physician-office laboratories. We believe that hospital-affiliated laboratories account for approximately 60% of the market, commercial clinical laboratories approximately one-third and physician-office laboratories the balance.

Key Trends. There are a number of key trends that we expect to have a significant impact on the clinical testing business in the United States and on our business. These trends present both opportunities and risks. The recent economic slowdown may temporarily reduce industry growth rates. However, because clinical testing is an essential healthcare service and because of the key trends discussed below, we believe that the industry will continue to grow over the long term and that we are well positioned to benefit from the long-term growth expected in the industry.

Demographics. The growing and aging population is increasing the demand for clinical testing.

Increased testing. We believe that we have entered the decade of diagnostics, moving from greater focus on curative care to a greater recognition of the value of detection, prevention and personalized care. Physicians increasingly are relying on testing to help identify risk factors and symptoms of disease, the choice of therapeutic regimen and the evaluation of treatment results. Physicians, consumers and payers increasingly recognize the value of testing as a means to improve health and reduce the overall cost of healthcare through early detection and prevention.

Science and technology advances. Medical advances allow for more accurate and earlier diagnosis and treatment of diseases. Continuing research and development in the area of genomics is expected to yield new, more sophisticated and specialized tests. These advances also are spurring interest in and demand for personalized or tailored medicine, which relies on diagnostic and prognostic testing. In addition, pharmacogenetic testing increasingly is used as a parameter to help speed drug approval processes and to better focus therapy based on patient and tumor-specific genetic markers.

Health information technologies. Demand is growing toward comprehensive care management solutions that serve patients, payers and practitioners by improving access to patient data, increasing patient participation in care management, reducing medical errors and improving clinical outcomes. There is an increasing focus on interconnectivity, the ability to interact with other software and systems, and real time data aggregation. Electronic medical records and patient health records continue to grow.

Customer and payer consolidation. Our customers and payers, including physicians, health insurance plans, employers, pharmaceutical companies and other intermediaries, have been consolidating. We expect that this trend will continue. Consolidation is increasing customer and payer bargaining power, enhancing purchasing sophistication and encouraging internalization of testing.

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Highly competitive. The clinical testing industry remains fragmented, is highly competitive and is subject to new competition. Competition is growing from non-traditional competitors. New market entrants with extensive resources may make acquisitions or expand into our traditional areas of operations. We also are expanding into new diagnostic testing areas that are highly competitive.

Regulatory and policy environment. Government oversight of and attention to the healthcare industry in the United States is significant and may increase. There has been extensive discussion of healthcare reform. While it is not possible to predict whether change in U.S. government regulation of healthcare will occur, or the nature or impact of any such change, we believe that any such change should recognize the value and importance of diagnostic testing to patient care.

Globalization. There is a growing demand for healthcare services in emerging market countries. Opportunities are arising to participate in the restructuring or growth of the healthcare systems in these countries. Additionally, our customers are establishing positions outside the United States. Demographic changes globally may also create opportunities.

Customers and Payers. We provide testing services to a broad range of customers, with orders for clinical testing generally generated by physicians, hospitals and employers. In most cases, the customer that orders the testing is not responsible for the payments of services. We consider a party that refers a test to us a customer and a party that reimburses us a payer. Depending on the billing arrangement and applicable law, the payer may be (1) a third party responsible for providing health insurance coverage to patients, such as a health insurance plan, self-insured employer benefit fund, or the traditional Medicare or Medicaid program, (2) the patient or (3) the physician or other party (such as a hospital, another laboratory or an employer) who referred the testing to us.

The following table shows current estimates of the breakdown of the percentage of our total volume of requisitions and net revenues associated with our clinical testing business during 2008 applicable to each payer group:

	Requisition Volume as % of Total Volume	Net Revenues as % of Total Clinical Laboratory Testing Net Revenues
Traditional Medicare and Medicaid Programs	15% - 20%	15% - 20%
Physicians, Hospitals, Employers and Other Monthly-Billed Clients	30% - 35%	20% - 25%
Health Plans: Fee-for-Service	30% - 35%	40% - 45%
Health Plans: Capitated	15% - 20%	5% - 10%
Patients	2% - 5%	5% - 10%

Health plans, including managed care organizations and other health insurance providers, typically reimburse us as a contracted provider on behalf of their members for clinical testing services performed. Reimbursement from our two largest health insurer payers totaled approximately 13% of our net revenues in 2008. Aetna, which accounted for over 7% of our consolidated net revenues for 2008, was our largest health insurer payer.

Physicians. Physicians requiring testing for patients are the primary referral source of our clinical testing volume. Physicians determine which laboratory to recommend or use, based on a variety of factors, including: service; patient access and convenience, including inclusion in a health plan network; price; and depth and breadth of test and service offering. Physicians also order our point-of-care tests.

Most of our clinical testing is referred by primary care physicians. We historically have provided a strong value proposition in routine and esoteric clinical testing. In 2007, we acquired AmeriPath, expanding our service capabilities. This will enable us to leverage our capabilities and to more effectively compete in several physician sub-specialties, including dermatology, urology, gastroenterology, hematology and oncology, where historically we had a smaller market share. We plan to continue to enhance our test menu and service capabilities.

Health Plans. Health plans typically negotiate directly or indirectly with a number of clinical laboratories, and represent approximately one-half of our total clinical testing volumes and one-half of our net revenues from clinical testing. In certain markets, such as California, health plans may delegate to independent physician associations (IPAs) the ability to negotiate for clinical testing services on behalf of certain members. The trend of consolidation among health plans has continued.

Health plans and IPAs often require that clinical test service providers accept discounted fee structures or assume all or a portion of the financial risk associated with providing testing services through capitated payment arrangements and discounted fee-for-service arrangements. Under capitated payment arrangements, we provide services at a predetermined monthly reimbursement rate for each covered member, generally regardless of the number or cost of services provided by us. Average reimbursement rates under capitated payment arrangements are typically lower than our overall average reimbursement rate. Health plans continue to focus product offerings on point-of-service (POS) plans, and consumer driven health plans (CDHPs) that offer a greater choice of healthcare providers. Reimbursement under these programs is typically negotiated on a fee-for-service basis, which generally results in higher revenue per requisition than under capitation arrangements. In addition, several health plans have made strategic acquisitions or have developed products to more broadly serve the individual (non-group) market. We do not expect that the design of these plans will pose a significant barrier to accessing clinical testing services. Increased number of patients in CDHPs and high deductible plans, such as those offered in the individual market, involve greater patient cost-sharing; this could negatively impact patient collection experience.

Most of our agreements with major health plans are non-exclusive arrangements. Certain health plans, however, have limited their laboratory network to only a single national laboratory to obtain improved pricing. In cases where members choose to use a non-contracted provider due to service, quality or convenience, the non-contracted provider is generally reimbursed at rates considered reasonable and customary. Contracted rates are generally lower than reasonable and customary rates because of the potential for greater volume as a contracted provider. A non-contracted clinical test service provider with quality and service preferred by physicians and patients to that of contracted providers may realize greater profits than if it were a contracted provider, if physicians and patients continue to have choice in selecting their clinical test provider and any potential additional cost to the patient of using a non-contracted provider is not considered prohibitive.

We also may be a member of a complementary network. A complementary network is generally a set of contractual arrangements that a third party will maintain with various providers that allow for discounted fees for the benefit of members of the customers that arrange access through the third party. A member of a health plan may choose to access a non-contracted provider that is a member of a complementary network; if so, the provider will be reimbursed at a rate negotiated by the complementary network.

We attempt to strengthen our relationships with health plans and increase the volume of testing services by offering health plans services and programs that leverage our Company s expertise and resources, including in such areas as wellness and disease management.

Hospitals and Other Laboratories. Hospitals generally maintain an on-site laboratory to perform the significant majority of clinical testing for their patients and refer less frequently needed and highly specialized procedures to outside laboratories, which typically charge the hospitals on a negotiated fee-for-service basis. Fee schedules for hospital reference testing typically are negotiated on behalf of hospitals by group purchasing organizations. We provide services to hospitals throughout the United States, including esoteric testing, helping manage their laboratories and serving as the medical directors of the hospital s histology or clinical laboratory. We believe that we are the industry s market leader in servicing hospitals. Hospitals generally continue to look for ways to fully utilize their existing laboratory capacity: they perform tests their patients need and compete with commercial laboratories for outreach (non-hospital patients) testing. Continuing to obtain referrals from hospitals depends on our ability to provide high quality services that are more cost-effective than if the hospitals were to perform the services themselves. We believe that our combination of full-service, bi-coastal esoteric testing capabilities, medical and scientific professionals available for consultation, innovative connectivity products, point-of-care testing products, focus on Six Sigma quality and dedicated sales and service professionals has positioned us to be an attractive partner for hospital customers.

Most physicians have admitting privileges or other relationships with hospitals as part of their medical practice. Many hospitals seek to leverage their relationships with community physicians by encouraging the physicians to send their outreach testing to the hospital s laboratory. In addition, hospitals that own physician practices generally require the physicians to refer tests to the hospital s affiliated laboratory. Hospitals can have greater leverage with health insurers than do commercial clinical laboratories, particularly hospitals that have a significant market share; hospitals thus are frequently able to negotiate higher reimbursement rates with health insurance plans than commercial clinical laboratories for comparable clinical testing services.

We also have joint venture arrangements with leading integrated healthcare delivery networks in several metropolitan areas. These joint venture arrangements, which provide testing for affiliated hospitals as well as for unaffiliated physicians and other local healthcare providers, serve as our principal laboratory facilities in their service areas. Typically, we have either a majority ownership interest in, or day-to-day management responsibilities for, our hospital joint venture relationships.

We also provide testing services to federal, state and local governmental agencies, and perform esoteric testing services for other commercial clinical laboratories that do not have a full range of testing capabilities. These customers are charged on a fee-for-service basis.

Employers. Employers use clinical tests for drugs-of-abuse to determine an individual s employability and his or her fitness for duty. Companies with high turnover and safety conscious environments provide the highest volumes of testing. Factors such as the general economy and job market can impact the utilization of clinical testing. We seek to grow our employer volumes through offering new and innovative programs to help companies with their goal in maintaining a safe and productive workplace. We also offer employers our Blueprint for Wellness program, providing wellness screenings to employers for their employees, to help employers manage increasing healthcare costs and to capitalize on trends in personalized health.

GENERAL

Competition. While there has been significant consolidation in the clinical testing industry in recent years, our industry remains fragmented and highly competitive. We primarily compete with three types of clinical testing providers: hospital-affiliated laboratories, other commercial clinical laboratories and physician-office laboratories. Our largest independent clinical laboratory competitor is Laboratory Corporation of America Holdings, Inc. In addition, we compete with many smaller regional and local commercial clinical laboratories, specialized esoteric laboratories and laboratories owned by physicians and hospitals. In anatomic pathology, additional competitors include anatomic pathology practices, including those in academic institutions. In addition, there has been a trend among specialty physician practices to bring pathologists into those practices.

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

service capability and quality;

accuracy, timeliness and consistency in reporting test results;

pricing;

patient insurance coverage;

number and type of tests performed by the provider;

number, convenience and geographic coverage of patient service centers;

reputation in the medical community;

healthcare information technology solutions;

qualifications; and

ability to develop new and useful tests.

We believe that we are an effective competitor in each of these areas. We also believe that the differentiation we are creating through our focus on providing the most comprehensive test menu, innovative test and information technology offerings, a superior patient experience, Six Sigma quality and unparalleled access and distribution provides us with a competitive advantage and enables us to compete on more than price alone.

We believe that large commercial clinical laboratories may be able to increase their share of the overall clinical 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 testing industry will continue. However, a significant portion of clinical testing is likely to continue to be performed by hospitals, which generally have affiliations with community physicians that refer testing to us. 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. In addition, recent market activity, including actions by payers to exclude large national clinical laboratories from contracts, may enhance the relative competitive position of regional laboratories.

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) point-of-care tests that can be performed by physicians in their offices; (2) complex 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. With our point-of-care test strategy, we are positioning ourselves to service this market for physicians and hospitals. We also believe that our overall point-of-care test 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.

The diagnostic product market is highly competitive. We have many competitors, some of which have much more extensive experience in this market and some of which have greater resources. We compete in this area by attempting to find and exploit unique differentiated products, including products that take advantage of our healthcare information technology solutions. There is no guarantee that we will be able to compete successfully in this market.

Sales and Marketing. Our sales force is organized to focus on customer groups and service types. The majority of representatives focus on marketing clinical laboratory testing, anatomic pathology and related services to physicians, including physician specialists. Supporting our physician sales teams are genomics and esoteric testing specialists, who are specially trained and focused on educating our clients on new and more complex tests. In addition, we have a health plan sales organization that focuses on regional and national insurance and healthcare organizations. We also have a hospital sales organization that focuses on meeting the unique clinical testing needs of hospitals and promotes the specialized capabilities of our Nichols Institute esoteric testing laboratories and our Focus Diagnostics infectious and immunologic disease testing laboratory. A smaller portion of our sales force focuses on selling drugs-of-abuse and wellness testing to employers. We also have a sales force that focuses on selling risk assessment testing services to life insurance companies. In addition, we have a sales organization that focuses on selling diagnostic products to hospitals, commercial clinical laboratories, physician office laboratories, blood banks and clinics, and a sales force that sells our point-of-care tests to customers globally. We also have a sales force that focuses on our clinical trials services to drug developers. We focus our sales efforts on obtaining and retaining profitable accounts. We have an active customer management process to evaluate the growth potential and profitability of all accounts.

Information Technology. Information systems are used extensively in virtually all aspects of our business, including clinical laboratory testing, test reporting, billing, customer service, logistics and management of medical data. We endeavor to establish systems that create value and efficiencies for our patients and customers. The successful delivery of our services depends, in part, on the continued and uninterrupted performance of our information technology systems.

We believe that our healthcare information technology systems help differentiate us favorably. Innovations in our healthcare information technology have the potential to improve patient care, promote efficiency and reduce expense. Both at the federal and state levels, there are public and private efforts to bring together healthcare providers, information technology vendors and other stakeholders to facilitate the creation of standards for the exchange and use of electronic healthcare data, including standard clinical code sets.

Some of our historic growth has come through acquisitions and we continue to use non-standardized billing, laboratory or other core information systems. We have standardized some of our systems and are implementing standard laboratory information and billing systems across our operations, including those from our most recent acquisitions. We expect implementation will take several more years to complete, and will result in significantly more centralized systems, improve operating efficiency, provide management with more timely and comprehensive information and enhance control over our operational environment.

Quality Assurance. In our clinical testing business, our goal is to continually improve the processes for collection, storage and transportation of patient specimens, as well as the precision and accuracy of analysis and result reporting. Our quality assurance efforts focus on positive patient identification of specimens and reports, proficiency testing, process audits, statistical process control and personnel training for all of our laboratories and patient service centers. We also focus on the licensing, credentialing, training and competency of our professional and technical staff. We are implementing an enhanced specimen tracking system, with global positioning system capabilities, that will enable us to better track specimens. We continue to implement our Six Sigma and standardization initiatives to help achieve our goal of becoming recognized as the undisputed quality leader in the healthcare services industry. In addition, some of our laboratories have achieved International Organization for Standardization, or ISO, certification. These certifications are international standards for quality management systems.

As part of our comprehensive quality assurance program, we have internal proficiency testing, extensive quality control and rigorous process audits for our clinical laboratory operations. For most clinical laboratory tests, quality control samples are processed in parallel with the analysis of patient specimens. The results of tests on these quality control samples are monitored to identify trends, biases or imprecision in our analytical processes.

We participate in external proficiency testing and have accreditation for our clinical laboratory operations from various regulatory agencies, such as CMS, the College of American Pathologists (CAP) and certain states. All of our laboratories participate in various external quality surveillance programs. They include, but are not limited to, proficiency testing programs administered by CAP, as well as some state agencies. CAP is an independent, non-governmental

organization of board-certified pathologists approved by CMS to inspect clinical laboratories to determine compliance with the standards required by the Clinical Laboratory Improvement Amendments of 1988 (CLIA). CAP offers an accreditation program to which laboratories may voluntarily subscribe. All of our major regional and esoteric laboratories, including our recently-opened facility in India, and most of our rapid response laboratories, are accredited by CAP. Accreditation includes on-site inspections and participation in the CAP (or equivalent) proficiency testing program. Also, all of our cytotechnologists and pathologists participate in an individual proficiency testing program.

Our diagnostic products businesses, Focus Diagnostics, Enterix and HemoCue, maintain extensive quality assurance programs focused on compliance with applicable regulatory requirements in the United States, Europe and Australia. They are regulated by the FDA and are required to be in compliance with the Quality Systems Regulations, 21 CFR part 820. In addition, they maintain sites certified in accordance with, or audited by the deemed authority for, ISO 13485: 2003 standards. We endeavor to design and manufacture our diagnostics products in compliance with Quality Systems Regulations so that the finished products are safe and effective. In addition, the diagnostics products businesses maintain procedures designed to ensure that products we purchase conform to the manufacturer s specifications.

Intellectual Property Rights. We own significant intellectual property, including patents, patent applications, technology, trade secrets, know-how, copyrights and trademarks in the United States and other countries. From time to time, we also license U.S. and non-U.S. patents, patent applications, technology, trade secrets, know-how, copyrights or trademarks owned by others. In the aggregate, these intellectual property assets and licenses are of material importance to our business. We believe, however, that no single patent, technology, trademark, intellectual property asset or license is material to our business as a whole.

Our approach is to manage our intellectual property assets to safeguard them and to maximize their value to our enterprise. We generally actively defend our intellectual property assets and pursue protection of our products, processes and other intellectual property where possible.

Our success in remaining a leading innovator in the diagnostic testing industry by continuing to introduce new tests, technology and services will depend, in part, on our ability to license new and improved technologies on favorable terms. Other companies or individuals, including our competitors, may obtain patents or other property rights on tests or processes that we may be performing, particularly in such emerging areas as gene-based testing and other specialty testing, that could prevent, limit or interfere with our ability to develop, perform or sell our tests or operate our business.

Employees. At December 31, 2008, we employed approximately 42,800 people. This total excludes employees of the joint ventures where we do not have a majority interest. We have no collective bargaining agreements with any unions covering any employees in the United States, and we believe that our overall relations with our employees are good.

BILLING AND REIMBURSEMENT

Billing. We generally bill for clinical testing services on a fee-for-service basis under one of two fee schedules. These fees are generally subject to negotiation with or discounted to non-governmental payers. The fee schedules are:

Client fees charged to physicians, hospitals, and institutions for which a clinical laboratory performs testing services on a wholesale basis and which are billed on a monthly basis.

Patient fees charged to individual patients and third-party payers, like Medicare and Medicaid.

Billing for clinical testing services is very complicated, and we have compliance policies and procedures that increase our billing costs. Patients, insurance companies, Medicare, Medicaid, physicians, hospitals and employer groups all have different billing requirements. Billing arrangements require us to bill various payers, and there are several other factors that complicate billing (e.g., disparity in coverage and information requirements among various payers; incomplete or inaccurate billing information provided by ordering physicians). We incur additional costs as a result of our participation in Medicare and Medicaid programs because clinical laboratory testing and anatomic pathology services are subject to complex, stringent and frequently ambiguous federal and state laws and regulations, including those relating to billing and reimbursement. Changes in laws and regulations could further complicate our billing and increase our billing expense. CMS establishes procedures and continuously evaluates and implements changes to the reimbursement process.

In 2008, our bad debt expense was 4.5% of our net revenues. We believe that most of our bad debt expense is primarily the result of missing or incorrect billing information on requisitions and Advance Beneficiary Notices (ABNs) 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. Deteriorating economic conditions may adversely impact our bad debt expense. In general, we perform the requested tests and report test results regardless of whether the billing information is correct or complete. We subsequently attempt to contact the healthcare provider or patient to obtain any missing information and to 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. The increased use of electronic ordering reduces the incidence of missing or incorrect information.

Billing Compliance. As an integral part of our billing compliance program, we investigate reported failures or suspected failures to comply with federal and state healthcare reimbursement requirements. Any Medicare or Medicaid overpayments resulting from non-compliance are reimbursed by us. As a result of these efforts, we have periodically identified and reported overpayments, reimbursed the overpayments and taken appropriate corrective action.

Penalties for violations of laws relating to billing federal healthcare programs and for violations of federal and state fraud and abuse laws include: (1) exclusion from participation in Medicare/Medicaid programs; (2) asset forfeitures; (3) civil and criminal fines and penalties; and (4) the loss of various licenses, certificates and authorizations necessary to operate our business. Civil monetary penalties for a wide range of violations may be assessed on a per violation basis. A parallel civil remedy under the federal False Claims Act provides for damages on a per violation basis, plus damages of up to three times the amount claimed.

Government Reimbursements. The healthcare industry has experienced significant changes in reimbursement practices during the past several years. Government payers, such as Medicare and Medicaid, have taken steps and can be expected to continue to take steps to control the cost, utilization and delivery of healthcare services, including clinical test services. With regard to the clinical test services performed on behalf of Medicare beneficiaries, we must bill the Medicare program directly and must accept the carrier s fee schedule amount as payment in full. In addition, state Medicaid programs are prohibited from paying more (and in most instances, pay significantly less) than Medicare. Currently, Medicare does not require the beneficiary to pay a co-payment for clinical laboratory testing. Certain Medicaid programs require Medicaid recipients to pay co-payment amounts for clinical laboratory testing. Medicare patients generally are required to make co-payments for anatomic pathology services.

Federal law contains a Medicare fee schedule payment methodology for clinical testing services performed for patients covered under Part B of the Medicare program, and a national ceiling on the amount that carriers could pay under their local Medicare fee schedules. Effective January 1, 2009, the national fee schedule for clinical testing services was increased 4.5%. Federal law also contains a Medicare fee schedule payment methodology for pathology and other physician services performed for patients covered under Part B of the Medicare program. Effective January 1, 2009, the national fee schedule for physician fees was increased 1.1%. If Medicare fee schedules are reduced, or if independent clinical laboratories are prohibited from billing Medicare directly for certain services, such as the technical component of pathology services provided to hospitals, it could have a material adverse effect on our business.

We are generally permitted to bill Medicare beneficiaries directly for statutorily excluded clinical testing services. An advance beneficiary notice (ABN) is a notice signed by the beneficiary which documents the patient s informed decision to personally assume financial liability for clinical tests which are likely to be denied and not reimbursed by Medicare because they are deemed to be not medically necessary (these tests include limited coverage tests for which the ordering physician did not provide an appropriate diagnosis code and certain tests ordered on a patient at a frequency greater than covered by Medicare). If a Medicare beneficiary signs an ABN, we are also generally permitted to bill the beneficiary for clinical tests that Medicare does not cover due to medical necessity limitations. We do not have any direct contact with most of these patients and, in such cases, cannot control the proper use of the ABN by the physician or the physician s office staff, who must obtain the ABN on our behalf. If the ABN is not timely provided to the beneficiary or is not completed properly, we may end up performing tests that we cannot subsequently bill to the patient if payment is denied by Medicare due to coverage limitations. CMS has issued manual changes requiring ABNs to include a specific price estimate for tests covered by ABNs. As a result, incorrectly completed forms could increase, resulting in more invalid ABNs and more tests that we cannot bill to the patient.

Clinical laboratories that bill Medicare or Medicaid could be excluded from participation in any federal healthcare programs if it is determined that without good cause they have submitted bills or requests for payment for items or services substantially in excess of the laboratory s usual charges for such items or services. The Department of Health and Human Services Office of Inspector General has periodically proposed to define the terms substantially in excess and usual charges, but has not finalized definitions of these terms.

CMS is permitted to adjust statutorily prescribed fees for clinical test services if the standard rules by which those payments are calculated will result in fees that are grossly excessive. CMS rules set forth a process and factors for establishing a realistic and equitable payment amount for clinical test services under Medicare Part B (and services paid under a prospective payment system) if existing payment amounts are determined to be inherently unreasonable; payment amounts may be considered unreasonable if they are either grossly excessive or deficient. Under CMS rules, if CMS or a carrier determines that an overall payment adjustment of less than 15% is needed to produce a realistic and equitable payment amount, then the payment amount is not considered grossly excessive or deficient. However, if a determination is made that a payment adjustment of 15% or more is justified, CMS could provide an adjustment of less than 15%, but not more than 15%, in any given year. Fees payable by Medicare could be reduced prospectively as a result of the application of these rules.

Historically, most Medicare and Medicaid beneficiaries were covered under the traditional Medicare and Medicaid programs directly administered by the federal government. Over the last several years, the federal government has sponsored programs to expand private health insurance options for Medicare beneficiaries and has encouraged such beneficiaries to switch from the traditional programs to the private programs, called Medicare Advantage programs. There has been rapid growth of health insurance plans offering Medicare Advantage programs and of beneficiary enrollment in these plans. In recent years, in an effort to control costs, states also have increasingly mandated that Medicaid beneficiaries enroll in private managed care arrangements. If these efforts continue to be successful, we may experience a further shift of traditional Medicare and Medicaid beneficiaries to private health insurance options.

Reduced Utilization of Clinical Testing. Government payers, such as Medicare and Medicaid, have taken steps and may continue to take steps to control the utilization and delivery of healthcare services, including clinical test services. Medicare carriers have adopted policies under which they do not pay for many commonly ordered clinical tests unless the ordering physician has provided an appropriate diagnosis code supporting the medical necessity of the test. Physicians are required by law to provide diagnostic information when they order clinical tests for Medicare and Medicaid patients.

Medicare Administrative Contractors. Historically, many different local intermediaries administered Medicare Part A and many different local carriers administered Medicare Part B (which covers services provide by independent clinical laboratories). They often had inconsistent policies, increasing the complexity of the billing process for clinical laboratories. They are being replaced with contractors who will handle both Part A and Part B. It is expected that the revised system will reduce the administrative complexity of billing for services provided to Medicare beneficiaries.

REGULATION

Our businesses are subject to or impacted by extensive and frequently changing laws and regulations, including inspections and audits by governmental agencies, in the United States (at both the federal and state levels) and the other jurisdictions in which we engage in these businesses. We also must comply with other laws and regulations that apply to conducting business generally (e.g., export controls laws, U.S. Foreign Corrupt Practices Act and similar laws of other jurisdictions), including in the United States and in the other jurisdictions in which we engage in business. Set forth below are highlights of the key regulatory areas applicable to our businesses.

CLIA and State Clinical Laboratory Licensing Regulations. All of our laboratories and, where applicable, patient service centers are licensed and accredited as required by the appropriate federal and state agencies. CLIA regulates virtually all clinical laboratories by requiring that they be certified by the federal government and comply with various operational, personnel and quality requirements intended to ensure that the services provided are accurate, reliable and timely. The cost of compliance with CLIA makes it cost prohibitive for many physicians to operate clinical laboratories in their offices. However, manufacturers of laboratory equipment and test kits could seek to increase their sales by marketing point-of-care test equipment to physicians and by selling to both physicians and patients test kits approved by the FDA for home use. Diagnostic tests approved or cleared by the FDA for home use are automatically deemed to be waived tests under CLIA and may be performed in physician office laboratories with minimal regulatory oversight under CLIA as well as by patients in their homes.

CLIA does not preempt state laws that are more stringent than federal law. State laws may require additional personnel qualifications, quality control, record maintenance and/or proficiency testing. State laws also may require detailed review of our scientific validations and technical procedures for each test before approval for use or marketing of services.

Fraud and Abuse Rules. Federal anti-kickback laws and regulations prohibit making payments or furnishing other benefits to influence the referral of tests billed to Medicare, Medicaid or certain other federal or state healthcare programs. The penalties for violation of these laws and regulations may include monetary fines, criminal and civil penalties and/or suspension or exclusion from participation in Medicare, Medicaid and other federal healthcare programs. Several states have similar laws.

In addition, federal anti-self-referral laws and the laws of some states generally prohibit Medicare and Medicaid payments for clinical tests referred by physicians who have a personal investment in, or a compensation arrangement with, the testing laboratory. Some states have similar anti-self-referral and other laws that are not limited to Medicare and Medicaid referrals and could also affect investment and compensation arrangements with physicians.

Drug Testing. The Substance Abuse and Mental Health Services Administration (SAMHSA) regulates drug testing for public sector employees and employees of certain federally regulated businesses. All laboratories that perform such testing must be certified as meeting SAMHSA s detailed performance and quality standards. All of our laboratories that perform such testing are so certified.

Medical Waste, Hazardous Waste and Radioactive Materials. Clinical laboratories in the United States are subject to federal, state and local regulations relating to the handling and disposal of regulated medical waste, hazardous waste and radioactive materials. We generally use outside vendors to dispose of such waste and contractually require them to comply with applicable laws and regulations.

FDA. The FDA has regulatory responsibility, among other things, over instruments, test kits, reagents and other devices used to perform diagnostic testing by clinical laboratories in the United States. The FDA also regulates clinical trials (and, therefore, testing that we perform for sponsors of those trials), drugs-of-abuse testing for employers, testing for blood bank purposes and testing of donors of human cells for purposes such as *in vitro* fertilization. A number of esoteric tests that are developed internally are first offered as laboratory-developed tests (LDTs). In the past, the FDA has claimed regulatory authority over all LDTs, but stated that it is exercising enforcement discretion in not regulating most LDTs performed by high complexity CLIA-certified laboratories. However, the FDA has been petitioned to exercise regulatory authority over certain LDTs and to initiate enforcement action against companies that make effectiveness claims about LDTs that are without sufficient analytical and clinical support. In addition, the FDA has issued two drafts of a guidance document describing certain LTDs as In Vitro Diagnostic Multivariate Index Assays. The FDA could finalize this guidance document, clarifying its intention to regulate these tests as medical devices and the laboratories that offer this subset of LDTs. If FDA regulation of this subset of LDTs occurs or if regulation of the various medical devices used in laboratory-developed testing ensues, it would lead to an increased regulatory burden resulting in additional costs and delays in introducing new tests, including genetic tests; this may hinder us from developing and marketing certain new products or services.

In September 2007, the FDA finalized its Guidance relating to Analyte Specific Reagents (ASRs), which laboratories use in their LDTs. As a result, manufacturers of certain products previously marketed as ASRs must file for FDA clearance of these products in order to market them in the United States. Failure to act diligently and to cooperate with the FDA may result in enforcement action against the manufacturer. The increased regulation of these products could result in increased product cost, a delay in obtaining them or, if a manufacturer withdraws its products from the market, an inability to obtain the product. These factors may hinder us from developing and marketing new products or services or cause us to have to increase the cost of our products or services.

Our diagnostic product business is subject to regulation by the FDA, as well as by foreign governmental agencies, including countries within the European Union who have adopted the Directive on In Vitro Diagnostic Medical Devices (IVDD). These agencies enforce laws and regulations that govern the development, testing, manufacturing, labeling, advertising, marketing, distribution and market surveillance of diagnostic products. Prior to marketing or selling most diagnostic products, currently we are required to secure clearance or approval from the FDA and (when appropriate) counterpart non-U.S. regulatory agencies, although the IVDD allows us to market in Europe many products using a process in which the manufacturer certifies that the device conforms to the regulatory and quality requirements for the device. Following the introduction of a diagnostic product into the market, the FDA and non-U.S. agencies engage in periodic reviews of the manufacturing processes and product performance. Compliance with these regulatory controls can affect the time and cost associated with the development, introduction and continued availability of new products. These agencies possess the authority to take various administrative and legal actions against us for non-compliance, such as fines, product suspensions, submission of warning letters, recalls, product seizures, injunctions and other civil and criminal sanctions. Where appropriate, voluntary compliance actions, such as voluntary recalls, may be undertaken.

Occupational Safety. The federal Occupational Safety and Health Administration (OSHA) has established extensive requirements relating specifically to workplace safety for healthcare employers in the United States. This includes requirements to develop and implement multi-faceted programs to protect workers from exposure to blood-borne pathogens, such as HIV and hepatitis B and C, including preventing or minimizing any exposure through sharps or needle stick injuries.

Transportation. For purposes of transportation, some biological materials and laboratory supplies are classified as hazardous materials and are subject to regulation by one or more of the following agencies: the U.S. Department of Transportation, the U.S. Public Health Service, the United States Postal Service and the International Air Transport Association.

Corporate Practice of Medicine. Many states, including some in which our businesses are located, prohibit business corporations from engaging in the practice of medicine. In certain states, business corporations are prohibited from employing licensed healthcare professionals to provide services on behalf of the corporation; these laws vary from state to state. The manner in which licensed physicians can be organized to perform medical services may be governed by the laws of the state in which medical services are provided and by the medical boards or other entities authorized by these states to oversee the practice of medicine. In some states, anatomic pathology services are delivered through physician-owned entities that employ the practicing pathologists.

Contracts and Relationships with Physicians. In our anatomic pathology business, we employ pathologists. Many of our pathologists enter into an employment agreement. These agreements have varying terms, but generally can be terminated at any time, upon advance notice. Most of the agreements contain covenants generally limiting the activities of the pathologist within a defined geographic area for a limited period of time after termination of employment. The agreements may be subject to limitations under state law that may limit the enforceability of these covenants.

Our pathologists are required to hold a valid license to practice medicine in the jurisdiction in which they practice. If they provide inpatient services, they must become a member of the medical staff at the relevant hospital, with privileges in pathology.

Fee-Splitting. Some states restrict the splitting or sharing of fees between physicians and non-physicians. These laws may apply to some of the arrangements that we have with pathologists; the laws vary from state to state.

Privacy and Security of Health and Personal Information; Standard Transactions. Healthcare providers and others involved in providing healthcare services to patients are required to comply with the federal Health Insurance Portability and Accountability Act (HIPAA) regulations regarding protecting the security and privacy of certain healthcare information, as well as HIPAA standards for electronic healthcare transactions in the United States. The HIPAA regulations on adoption of national provider identifiers required healthcare providers to adopt new, unique identifiers for reporting on claims transactions. The security regulations establish requirements for safeguarding electronic patient information. The privacy regulations establish comprehensive federal standards regarding the uses and disclosures of protected health information. The regulations establish a complex regulatory framework on a variety of subjects. We have implemented practices to meet the requirements of the regulations.

We also must comply with privacy and security laws and regulations adopted by states in the United States and jurisdictions outside the United States in which we conduct business, including the European Union. Some of these laws and regulations relate to the privacy and security of personal information, such as social security numbers. Some of the laws and regulations impose reporting and disclosure requirements in the event of certain security breaches. We have implemented practices to meet applicable requirements.

Controlled Substances. The federal Drug Enforcement Administration (DEA) regulates access to controlled substances used to perform drugs-of-abuse testing in the United States. To obtain access to controlled substances, laboratories must be licensed by the DEA. All of our laboratories in the United States that use controlled substances are licensed by the DEA.

Compliance. We seek to conduct our business in compliance with all applicable laws and regulations. Many of the laws and regulations applicable to us, however, including those relating to billing and reimbursement of tests and those relating to relationships with physicians and hospitals, are vague or indefinite and have not been interpreted by the courts. They may be interpreted or applied by a prosecutorial, regulatory or judicial authority in a manner that could require us to make changes in our operations, including our pricing and/or billing practices. The applicability or interpretation of laws and regulations also may not be clear in light of emerging changes in clinical testing science and healthcare technology. Such occurrences, regardless of their outcome, could, among other things:

- increase our operating costs including, but not limited to, those costs associated with performing clinical or anatomic pathology tests or manufacturing or distributing products, and administrative requirements related to billing;
- decrease the amount of reimbursement related to testing services performed;
- damage our reputation; and/or
- adversely affect important business relationships with third parties.

If we fail to comply with applicable laws and regulations, we could suffer civil and criminal penalties, fines, exclusion from participation in governmental healthcare programs and the loss of various licenses, certificates and authorizations necessary to operate our business, as well as incur additional liabilities from third party claims, all of which could have a material adverse effect on our business. Certain federal and state statues, regulations and other laws, including the *qui tam* provisions of the federal False Claims Act, allow private individuals to bring lawsuits against healthcare companies on behalf of government payers, private payers and/or patients alleging inappropriate billing practices.

The federal or state governments may bring claims based on theories as to our current practices that we believe are lawful. The federal government has substantial leverage in negotiating settlements since the amount of potential damages far exceeds the rates at which we are reimbursed, and the government has the remedy of excluding a non-compliant provider from participation in the Medicare and Medicaid programs, which represented approximately 18% of our net revenues during 2008. We believe that, based on our experience with settlements and public announcements by

various government officials, the federal government continues to strengthen its enforcement efforts against healthcare fraud. In addition, legislative provisions relating to healthcare fraud and abuse provide federal enforcement personnel substantially increased funding, powers and remedies to pursue suspected cases of fraud and abuse.

We have a long-standing and well-established compliance program. The Quality, Safety & Compliance Committee of our Board of Directors oversees our compliance program and requires periodic management reports regarding our compliance program. Our program emphasizes the development of training programs intended to ensure the strict implementation and observance of all applicable laws, regulations and Company policies. Further, we conduct in-depth reviews of procedures and facilities to assure regulatory compliance throughout our operations. We conduct annual training of our employees on these compliance policies and procedures.

AVAILABLE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (the SEC). You may read and copy any document that we file with the SEC at the SEC s public reference room at 100 F Street, NE, Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for information regarding the public reference room. The SEC maintains an internet site that contains annual, quarterly and current reports, proxy and information statements and other information that issuers (including Quest Diagnostics) file electronically with the SEC. Our electronic SEC filings are available to the public at the SEC s internet site, www.sec.gov.

Our internet site is www.questdiagnostics.com. You can access Quest Diagnostics Investor Relations webpage at www.questdiagnostics.com/investor. We make available free of charge, on or through our Investor Relations webpage, our proxy statements, Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to those reports filed or furnished pursuant to the Securities Exchange Act of 1934, as amended (the Exchange Act), as soon as reasonably practical after such material is filed with, or furnished to, the SEC. We also make available, through our Investor Relations webpage, statements of beneficial ownership of our equity securities filed by our directors, officers, 10% or greater shareholders and others under Section 16 of the Exchange Act.

We have a corporate governance webpage. You can access information regarding our corporate governance at www.questdiagnostics.com/governance. We post the following on our corporate governance webpage:

Code of Business Ethics

Integrity Commitment

Values

Corporate Governance Guidelines

Charters for our Audit and Finance Committee, Compensation Committee, Executive Committee, Governance Committee and Quality, Safety and Compliance Committee

Certificate of Incorporation

Bylaws

You can request a copy of these documents, including exhibits, at no cost, by contacting Investor Relations, 3 Giralda Farms, Madison, New Jersey 07940 (973-520-2700). The information on our website is not incorporated by reference into this Report.

EXECUTIVE OFFICERS OF THE COMPANY

The following persons serve as executive officers of the Company.

Surya N. Mohapatra, Ph.D. (59) is Chairman of the Board, President and Chief Executive Officer. Prior to joining the Company in February 1999 as Senior Vice President and Chief Operating Officer, he was Senior Vice President of Picker International, a worldwide leader in advanced medical imaging technologies. Dr. Mohapatra was appointed President and Chief Operating Officer in June 1999, Chief Executive Officer in May 2004 and Chairman of the Board in December 2004. He is a director of ITT Corporation. Dr. Mohapatra has been a director of the Company since 2002.

Robert A. Hagemann (52) is Senior Vice President and Chief Financial Officer. He joined Corning Life Sciences, Inc. in 1992, where he held a variety of senior financial positions before being named Vice President and Corporate Controller of the Company in 1996. Mr. Hagemann has served as Chief Financial Officer since August 1998. He is a director of Zimmer Holdings, Inc.

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Joan E. Miller, Ph.D. (54) is Senior Vice President - Pathology and Hospital Services. Dr. Miller joined Corning Life Sciences, Inc. in 1992 and since has held positions of increasing responsibility. Dr. Miller was named Senior Managing Director, Nichols Institute in 2002 and Vice President, Hospital Business in 2003. Since June 2007, Dr. Miller has overseen the Company s hospital services business, including its esoteric testing facilities, and its anatomic pathology services business, including AmeriPath.

Michael E. Prevoznik (47) is Senior Vice President and General Counsel. Mr. Prevoznik joined the Company as Vice President and General Counsel in August 1999. In 2003, he assumed responsibility for governmental affairs. Prior to joining the Company, Mr. Prevoznik served in positions of increasing responsibility within the compliance organization at SmithKline Beecham, most recently as Vice President, Compliance, with responsibility for coordinating all SmithKline Beecham compliance activities worldwide.

Wayne R. Simmons (53) is Vice President - Operations. Since July 2007, he has overseen the Company s U.S. clinical testing operations. Mr. Simmons joined the Company in February 2004 as Vice President for our central region. Prior to joining the Company, Mr. Simmons served in positions of increasing responsibility with Philips Medical Systems, including, since 2002, as Vice President of Supply Chain, in which position he was responsible for operations at Philips Medical Systems CT Operations facilities globally.

Item 1A. Risk Factors

You should carefully consider all of the information set forth in this Report, including the following risk factors, before deciding to invest in any of our securities. The risks below are not the only ones that we face. Additional risks not presently known to us, or that we presently deem immaterial, may also negatively impact us. Our business, financial condition, results of operations or cash flows could be materially impacted by any of these factors.

This Report also includes forward-looking statements that involve risks or uncertainties. Our results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks we face described below and elsewhere. See Cautionary Factors that May Affect Future Results on page 28.

Recent changes in U.S., global, or regional economic conditions could have an adverse effect on our businesses.

The recent unprecedented level of volatility and disruption in the financial markets has adversely affected economic activity in the United States and other regions of the world in which we do business. The continued decline in economic conditions may adversely affect demand for our services and products, thus reducing our revenue. These conditions could also impair the ability of those with whom we do business to satisfy their obligations to us.

In addition, these conditions have increased uncertainty regarding the availability of, and terms of access to, external sources of capital. If we were unable to secure access to external capital over a sustained period of time or on reasonable terms, this could impair our ability to achieve our business objectives.

The clinical testing business is highly competitive, and if we fail to provide an appropriately priced level of service or otherwise fail to compete effectively it could have a material adverse effect on our net revenues and profitability.

While there has been significant consolidation in recent years in the clinical testing business, it remains a fragmented and highly competitive industry.

We primarily compete with three types of clinical test providers: hospital-affiliated laboratories, other independent clinical laboratories and physician-office laboratories. We also compete with anatomic pathology practices and large physician group practices. Hospitals generally maintain on-site laboratories to perform testing on their patients (inpatient or outpatient). In addition, many hospitals compete with independent clinical laboratories for outreach (non-hospital patients) testing. Most physicians have admitting privileges or other relationships with hospitals as part of their medical practice and hospitals may seek to leverage their relationships with community physicians and encourage the physicians to send their outreach testing to the hospital s laboratory. In addition, hospitals that own physician practices generally require the physicians to refer tests to the hospital s laboratory. As a result of this affiliation between hospitals and community physicians, we compete against hospital-affiliated laboratories primarily based on quality of service. Our failure to provide a broad test menu or service superior to hospital-affiliated laboratories and other laboratories could have a material adverse effect on our business.

If we fail to compete effectively, our business could be adversely affected and our net revenues and profitability could be damaged.

Our business could be adversely impacted if healthcare reform focuses on reducing healthcare costs but does not recognize the value and importance of diagnostic testing.

Government oversight of and attention to the healthcare industry in the United States is significant and may increase. There has been extensive public discussion of healthcare reform. While it is not possible to predict whether

change in U.S. government regulation of healthcare will occur, or the nature or impact of any such change, our business could be adversely impacted if healthcare reform focuses on reducing healthcare costs but does not recognize the value and importance of diagnostic testing.

Government payers, such as Medicare and Medicaid, have taken steps to control the utilization and reimbursement of healthcare services, including clinical test services.

We face efforts by government payers to reduce utilization and reimbursement for clinical testing services.

From time to time, Congress has legislated reductions in, or frozen updates to, the Medicare Clinical Laboratory Fee Schedule. In addition, CMS has adopted policies limiting or excluding coverage for clinical tests that we perform. We also provide physician services which are reimbursed by Medicare under a physician fee schedule, which is subject to adjustment on an annual basis. CMS changes add to our costs by increasing complexity and administrative requirements. Medicaid reimbursement varies by state and is subject to administrative and billing requirements and budget pressures.

In addition, over the last several years, the federal government has sponsored programs to expand private health insurance programs for Medicare beneficiaries, called Medicare Advantage programs, and has encouraged such beneficiaries to switch from the traditional programs to the private programs. There has been rapid growth of health insurance plans offering Medicare Advantage programs, and of beneficiary enrollment in these programs. Also in recent years, states have increasingly mandated that Medicaid beneficiaries enroll in private managed care arrangements. If these efforts continue to be successful, we may experience a further shift of traditional Medicare and Medicaid beneficiaries to private health insurance options. Recently, state budget pressures have encouraged states to consider several courses that may impact our business, such as delaying payments, reducing reimbursement, restricting coverage eligibility, service coverage restrictions and imposing taxes on our services.

From time to time, the federal government has considered whether competitive bidding can be used to provide clinical testing services for Medicare beneficiaries at attractive rates while maintaining quality and access to care. In 2008, Congress enacted legislation that eliminated a proposed competitive bidding demonstration project for clinical testing services. State governments also have considered from time to time whether to apply competitive bidding to clinical testing services. The industry remains concerned about the potential use of competitive bidding for clinical testing services and believes that the quality of services and access to those services could be adversely impacted by implementation of competitive bidding. If competitive bidding were implemented on a regional or national basis for clinical testing, it could materially adversely affect us.

We expect efforts to reduce reimbursements, to impose more stringent cost controls and to reduce utilization of clinical test services will continue. These efforts, including changes in law or regulations, may have a material adverse impact on our business.

Healthcare plans have taken steps to control the utilization and reimbursement of healthcare services, including clinical test services.

We also face efforts by non-governmental third party payers, including healthcare plans, to reduce utilization and reimbursement for clinical testing services.

The healthcare industry has experienced a trend of consolidation among healthcare insurance plans, resulting in fewer but larger insurance plans with significant bargaining power to negotiate fee arrangements with healthcare providers, including clinical laboratories. These healthcare plans, and independent physician associations, may demand that clinical laboratories accept discounted fee structures or assume all or a portion of the financial risk associated with providing testing services to their members through capitated payment arrangements. In addition, some healthcare plans have been willing to limit the PPO or POS laboratory network to only a single national laboratory to obtain improved fee-for-service pricing. There are also an increasing number of patients enrolling in consumer driven products and high deductible plans that involve greater patient cost-sharing.

The increased consolidation among healthcare plans also has increased the potential adverse impact of ceasing to be a contracted provider with any such insurer.

We expect continuing efforts to reduce reimbursements, to impose more stringent cost controls and to reduce utilization of clinical test services. These efforts, including future changes in third-party payer rules, practices and policies, or ceasing to be a contracted provider to a healthcare plan, may have a material adverse effect on our business.

Business development activities are inherently risky, and integrating our operations with businesses we acquire may be difficult and, if unsuccessfully executed, may have a material adverse effect on our business.

We plan selectively to enhance our business from time to time through business development activities, such as strategic acquisitions, licensing, investments and alliances. However, these plans are subject to the availability of appropriate opportunities and competition from other

companies seeking similar opportunities. Moreover, the success of

any such effort may be affected by a number of factors, including our ability to properly assess and value the potential business opportunity, and to integrate it into our business. The success of our strategic alliances depends not only on our contributions and capabilities, but also on the property, resources, efforts and skills contributed by our strategic partners. Further, disputes may arise with strategic partners, due to conflicting priorities or conflicts of interests.

Each acquisition involves the integration of a separate company that was previously operated independently and has different systems, processes, policies and cultures. Integration of acquisitions involves a number of risks including the diversion of management s attention to the assimilation of the operations of businesses we have acquired, difficulties in the integration of operations and systems and the realization of potential operating synergies, the assimilation and retention of the personnel of the acquired companies, challenges in retaining the customers of the combined businesses, and potential adverse effects on operating results. The process of combining companies may be disruptive to our businesses and may cause an interruption of, or a loss of momentum in, such businesses as a result of the following difficulties, among others:

- loss of key customers or employees;
- difficulty in standardizing information and other systems;
- difficulty in consolidating facilities and infrastructure;
- failure to maintain the quality of services that our Company has historically provided;
- diversion of management s attention from the day-to-day business of our Company as a result of the need to deal with the foregoing disruptions and difficulties; and
- the added costs of dealing with such disruptions.

If we are unable successfully to integrate strategic acquisitions in a timely manner, our business and our growth strategies could be negatively affected. Even if we are able to successfully complete the integration of the operations of other companies or businesses we may acquire in the future, we may not be able to realize all or any of the benefits that we expect to result from such integration, either in monetary terms or in a timely manner.

Our business could be negatively affected if we are unable successfully to continue to improve our efficiency.

As noted above, government payers and healthcare insurers have taken steps to control the utilization and reimbursement of healthcare services, including clinical testing services; such steps may continue. If we are unable to continue to improve our efficiency to enable us to mitigate the impact on our profitability of these activities, our business could be negatively affected.

Adverse resolution of the investigation related to NID may cause us material losses and have an adverse impact on our business and reputation.

NID and the Company each received a subpoena from the United States Attorney s Office for the Eastern District of New York during the fourth quarter of 2004. The subpoenas requested a wide range of business records, including documents regarding parathyroid hormone (PTH) test kits manufactured by NID and PTH testing performed by the Company. The Company has voluntarily and actively cooperated with the investigation, providing information, witnesses and business records of NID and the Company, including documents related to PTH tests and test kits, as well as other tests and test kits. In the second and third quarters of 2005, the FDA conducted an inspection of NID and issued a Form 483 listing the observations made by the FDA during the course of the inspection. NID responded to the Form 483.

During the third quarter of 2007, the government and the Company began settlement discussions. In the course of those discussions, the government disclosed to the Company certain of the government s legal theories regarding the amount of damages allegedly incurred by the government, which include alleged violations of civil and criminal statutes including the False Claims Act and the Food, Drug and Cosmetics Act. Violations of these statutes and related regulations could lead to a warning letter, injunction, fines or penalties, exclusion from federal healthcare programs and/or criminal prosecution, as well as claims by third parties. During the third quarter of 2008, the Company and the United States Attorney s Office reached an agreement in principle to resolve these claims. As part of the agreement, NID, which was closed in 2006, is expected to enter a guilty plea to a single count of felony misbranding. The terms of the settlement are subject to the final negotiation and execution of definitive agreements, which is expected to include a corporate integrity agreement, the approval by the United States Department of Justice and the United States Department of Health and Human Services and satisfactory resolution of related state claims. There can be no assurance, however, when or if a settlement may be finalized, or as to its terms. If a settlement is not finalized, the Company would defend itself and NID and could incur significant costs in doing so.

Any settlement is expected to include a corporate integrity agreement which may adversely impact our business operations and increase our costs.

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The Company has established a reserve reflected in discontinued operations of $316 million in connection with these claims. The reserve reflects the Company s current estimate of the expected probable loss with respect to these matters, assuming the settlement is finalized. If a settlement is not finalized, the eventual losses related to these matters could be materially different than the amount reserved and could be material to the Company s results of operations, cash flows and financial condition in the period that such matters are determined or paid.

We are subject to numerous legal and regulatory requirements governing our activities, and we may face substantial fines and penalties, and our business activities may be impacted, if we fail to comply.

Our business is subject to or impacted by extensive and frequently changing laws and regulations in the United States (including at both the federal and state levels), and the other jurisdictions in which we engage in business. While we seek to conduct our business in compliance with all applicable laws, many of the laws and regulations applicable to us are vague or indefinite and have not been interpreted by the courts, including those relating to:

billing and reimbursement of clinical tests;

certification of clinical laboratories;

the anti-self-referral and anti-kickback laws and regulations;

the laws and regulations administered by the U.S. Food and Drug Administration;

the corporate practice of medicine;

operational, personnel and quality requirements intended to ensure that clinical testing services are accurate, reliable and timely;

physician fee splitting;

relationships with physicians and hospitals;

safety and health of laboratory employees; and

handling, transportation and disposal of medical specimens, infectious and hazardous waste and radioactive materials.

These laws and regulations may be interpreted or applied by a prosecutorial, regulatory or judicial authority in a manner that could require us to make changes in our operations, including our pricing and/or billing practices. We may not be able to maintain, renew or secure required permits, licenses or any other regulatory approvals needed to operate our business or commercialize our products. If we fail to comply with applicable laws and regulations, or if we fail to maintain, renew or obtain necessary permits, licenses and approvals, we could suffer civil and criminal penalties, fines, exclusion from participation in governmental healthcare programs and the loss of various licenses, certificates and authorizations necessary to operate our business, as well as incur additional liabilities from third party claims. If any of the foregoing were to occur, our reputation could be damaged, important business relationships with third parties could be adversely affected and it could have a material adverse effect on our business.

We regularly receive requests for information, and occasionally subpoenas, from governmental authorities. We also are subject from time to time to qui tam claims brought by former employees or other whistle blowers. The federal and state governments continue to strengthen their position and scrutiny over healthcare fraud. In addition, legislative provisions relating to healthcare fraud and abuse provide federal enforcement personnel substantially increased funding, powers and remedies to pursue suspected fraud and abuse. The government has substantial leverage in negotiating settlements since the amount of potential damages far exceeds the rates at which we are reimbursed for our products and services, and the government has the remedy of excluding a non-compliant provider from participation in the Medicare and Medicaid programs, which represented approximately 18% of our net revenues for the year ended December 31, 2008. Regardless of merit or eventual outcome, these types of investigations and related litigation can result in:

diversion of management time and attention;

expenditure of large amounts of cash on legal fees, costs and payment of damages;

limitations on our ability to continue some of our operations;

enforcement actions, fines and penalties or the assertion of private litigation claims and damages;

decreased demand for our services and products; and/or

injury to our reputation.

Although we believe that we are in compliance, in all material respects, with applicable laws and regulations, there can be no assurance that a regulatory agency or tribunal would not reach a different conclusion. Any noncompliance by us with applicable laws and regulations could have a material adverse effect on our results of operations. Moreover, even when an investigation is resolved favorably, the process may be time-consuming and the legal costs and diversion of management focus may be extensive.

Changes in applicable laws and regulations may result in existing practices becoming more restricted, or subject our existing or proposed services and products to additional costs, delay, modification, withdrawal or reconsideration. Such changes could require us to modify our business objectives and could have a material adverse effect on our business.

Failure to timely or accurately bill for our services could have a material adverse effect on our business.

Billing for clinical testing services is extremely complicated and is subject to extensive and non-uniform rules and administrative requirements. Depending on the billing arrangement and applicable law, we bill various payers, such as patients, insurance companies, Medicare, Medicaid, physicians, hospitals and employer groups. Changes in laws and regulations could increase the complexity and cost of our billing process. Additionally, auditing for compliance with applicable laws and regulations as well as internal compliance policies and procedures adds further cost and complexity to the billing process. Further, our billing systems require significant technology investment and, as a result of marketplace demands, we need to continually invest in our billing systems.

Missing or incorrect information on requisitions adds complexity to and slows the billing process, creates backlogs of unbilled requisitions, and generally increases the aging of accounts receivable and bad debt expense. We believe that much of our bad debt expense in recent years is attributable to the lack of, or inaccurate, billing information. Failure to timely or correctly bill may lead to our not being reimbursed for our services or an increase in the aging of our accounts receivable, which could adversely affect our results of operations and cash flows. Failure to comply with applicable laws relating to billing federal healthcare programs could lead to various penalties, including: (1) exclusion from participation in Medicare/Medicaid programs; (2) asset forfeitures; (3) civil and criminal fines and penalties; and (4) the loss of various licenses, certificates and authorizations necessary to operate our business, any of which could have a material adverse effect on our results of operations or cash flows.

Failure in our information technology systems, including failures resulting from our systems conversions, could disrupt our operations and cause the loss of customers or business opportunities.

Information technology (IT) systems are used extensively in virtually all aspects of our business, including clinical testing, test reporting, billing, customer service, logistics and management of medical data. Our success depends, in part, on the continued and uninterrupted performance of our IT systems. IT systems may be vulnerable to damage from a variety of sources, including telecommunications or network failures, human acts and natural disasters. Moreover, despite the security measures we have implemented, our IT systems may be subject to physical or electronic break-ins, computer viruses and similar disruptive problems. We also have taken precautionary measures to prevent unanticipated problems that could affect our IT systems. Nevertheless, we may experience damages to our systems, and system failures and interruptions.

In addition, we are in the process of implementing standard laboratory information and billing systems, which we expect will take several years to complete. Failure to properly implement this standardization process could materially adversely affect our business. During system conversions of this type, workflow is re-engineered to take advantage of best practices and enhanced system capabilities, which may cause temporary disruptions in service. In addition, the implementation process, including the transfer of databases and master files to new data centers, presents significant conversion risks that need to be managed carefully.

If we experience systems problems, including with our implementation of standard laboratory or billing systems, they may interrupt our ability to operate. For example, the problems may impact our ability to process test orders, deliver test results or perform or bill for tests in a timely manner. If our operations are interrupted, it could adversely affect our reputation and result in a loss of customers and net revenues.

Failure to develop, or acquire licenses for, new tests, technology and services could negatively impact our testing volume and net revenues.

The diagnostics testing industry is faced with changing technology and new product introductions. Other companies or individuals, including our competitors, may obtain patents or other property rights that would prevent, limit or interfere with our ability to develop, perform or sell our tests or operate our business or increase our costs. In addition, they could introduce new tests that may result in a decrease in the demand for our tests or cause us to reduce the prices of our tests. Our success in continuing to introduce new tests, technology and services will depend, in part, on our ability to license new and improved technologies on favorable terms. We may be unable to develop or introduce new tests. We also may be unable to continue to negotiate acceptable licensing arrangements, and arrangements that we do conclude may not yield commercially successful diagnostic tests. If we are unable to license these testing methods at competitive rates, our

research and development costs may increase as a result. In addition, if we are unable to develop and introduce, or license, new tests, technology and services to expand our esoteric testing business, our testing methods may become outdated when compared with our competition and our testing volume and revenue may be materially and adversely affected.

We may be subject to intellectual property litigation that could adversely impact our business.

We may be subject to intellectual property litigation and we may be found to infringe on the proprietary rights of others, which could force us to do one or more of the following:

- cease developing, performing or selling products or services that incorporate the challenged intellectual property;
- obtain and pay for licenses from the holder of the infringed intellectual property right;
- redesign or reengineer our tests;
- change our business processes; or
- pay substantial damages, court costs and attorneys fees, including potentially increased damages for any infringement held to be willful.

The development of new, more cost-effective tests that can be performed by our customers or by patients, or the internalization of testing by hospitals or physicians, could negatively impact our testing volume and net revenues.

Advances in technology may lead to the development of more cost-effective tests that can be performed outside of an independent clinical laboratory such as (1) point-of-care tests that can be performed by physicians in their offices, (2) esoteric tests that can be performed by hospitals in their own laboratories or (3) home testing that can be performed by patients in their homes or by physicians in their offices. Although the CLIA compliance costs make it cost prohibitive for many physicians to operate clinical laboratories in their offices, manufacturers of laboratory equipment and test kits could seek to increase their sales by marketing point-of-care test equipment to physicians. Diagnostic tests approved or cleared by the FDA for home use are automatically deemed to be waived tests under CLIA and may be performed in physician office laboratories with minimal regulatory oversight under CLIA as well as by patients in their homes. Test kit manufacturers could seek to increase sales to both physicians and patients of test kits approved by the FDA for point-of-care testing or home use. Development of such technology and its use by our customers would reduce the demand for our laboratory-based testing services and negatively impact our net revenues.

Our customers, such as hospitals and physicians, may internalize tests that we currently perform. If our customers were to internalize tests that we currently perform and we did not develop new or alternative tests attractive to our customers, the demand for our testing services may be reduced and our net revenues may be materially adversely impacted.

Our outstanding debt may impair our financial and operating flexibility.

As of December 31, 2008, we had approximately $3.1 billion of long-term debt outstanding. Except for outstanding letters of credit and operating leases, we do not have any off-balance sheet financing arrangements in place or available. Our debt agreements contain various restrictive covenants. These restrictions could limit our ability to use operating cash flow in other areas of our business because we must use a portion of these funds to make principal and interest payments on our debt. We have obtained ratings on our debt from Standard and Poor s and Moody s Investor Services. There can be no assurance that any rating so assigned will remain for any given period of time or that a rating will not be lowered or withdrawn entirely by a rating agency if in that rating agency s judgment future circumstances relating to the basis of the rating, such as adverse changes in our Company or our industry, so warrant. If such ratings are lowered, the borrowing costs on our senior unsecured revolving credit facility, secured receivables facility and term loan would increase. Changes in our credit ratings, however, do not require repayment or acceleration of any of our debt.

We or our subsidiaries may incur additional indebtedness in the future. Our ability to make principal and interest payments will depend on our ability to generate cash in the future. If we incur additional debt, a greater portion of our cash flows may be needed to satisfy our debt service obligations and if we do not generate sufficient cash to meet our debt service requirements, we may need to seek additional financing. In this case, it may be more difficult, or we may be unable, to obtain financing on terms that are acceptable to us. As a result, we would be more vulnerable to general adverse economic, industry and capital markets conditions as well as the other risks associated with indebtedness.

Our ability to attract and retain qualified employees is critical to the success of our business and the failure to do so may materially adversely affect our performance.

Our people are a critical resource. The supply of qualified personnel may be limited and competition for qualified employees is strong. If we were to lose, or to fail to attract and retain, key management personnel or qualified

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skilled technical or professional employees at our clinical laboratories, research centers or manufacturing facilities, our earnings and revenues could be adversely affected. In addition, if we were to lose, or to fail to attract and retain, skilled pathologists with positive relationships with their respective local medical communities, particularly those with subspecialties, our earnings and revenues could be adversely affected.

Failure to establish, and perform to, appropriate quality standards to assure that the highest level of quality is observed in the performance of our testing services and in the design, manufacture and marketing of our products could adversely affect the results of our operations and adversely impact our reputation.

The provision of clinical testing services, including anatomic pathology services, and related services, and the design, manufacture and marketing of diagnostic products involve certain inherent risks. The services that we provide and the products that we design, manufacture and market are intended to provide information for healthcare providers in providing patient care. Therefore, users of our services and products may have a greater sensitivity to errors than the users of services or products that are intended for other purposes.

Manufacturing or design defects, unanticipated use of our products, or inadequate disclosure of risks relating to the use of the product can lead to injury or other adverse events. These events could lead to recalls or safety alerts relating to our products (either voluntary or required by governmental authorities) and could result, in certain cases, in the removal of a product from the market. Any recall could result in significant costs as well as negative publicity that could reduce demand for our products. Personal injuries relating to the use of our products can also result in product liability claims being brought against us. In some circumstances, such adverse events could also cause delays in new product approvals.

Similarly, negligence in performing our services can lead to injury or other adverse events. We may be sued under physician liability or other liability law for acts or omissions by our pathologists, laboratory personnel and hospital employees who are under the supervision of our hospital-based pathologists. We are subject to the attendant risk of substantial damages awards and risk to our reputation.

The failure of our IT systems to keep pace with technological advances may significantly reduce our revenues or increase our expenses.

Public and private initiatives to create healthcare information technology (HCIT) standards and to mandate standardized clinical coding systems for the electronic exchange of clinical information, including test results, could require costly modifications to our existing HCIT systems. While we do not expect HCIT standards to be adopted or implemented without adequate time to comply, if we fail to adopt or delay in implementing HCIT standards, we could lose customers and business opportunities.

Our operations and reputation may be impaired if we do not comply with privacy laws or information security policies.

In our business, we generate or maintain sensitive information, such as patient data. If we do not adequately safeguard that information and it were to become available to persons or entities that should not have access to it, our business could be impaired and our reputation could suffer.

We are subject to numerous political, legal, operational and other risks as a result of our international operations which could impact our business in many ways.

Although we conduct most of our business in the United States, our expanding international operations increase our exposure to the inherent risks of doing business in international markets. Depending on the market, these risks include, without limitation:

changes in the local economic environment;

political instability;

social changes;

intellectual property legal protections and remedies;

trade regulations;

procedures and actions affecting approval, production, pricing, reimbursement and marketing of products and services;

exchange controls;

weak legal systems which may affect our ability to enforce contractual rights;

changes in local laws or regulations; and

potentially longer payment and collection cycles.

International operations also require us to devote significant management resources to implement our controls and systems in new markets, to comply with the U.S. Foreign Corrupt Practices Act and similar laws in local jurisdictions and to overcome challenges based on differing languages and cultures.

We expect to expand further our international operations, through acquisition or otherwise, which would increase these risks. As a result of these risks, our financial condition or results of operations could be materially adversely affected.

Our medical diagnostic products business is subject to numerous governmental regulations and it can be costly to comply with these regulations and to develop compliant diagnostics products.

Our medical diagnostic products are subject to extensive regulation by numerous governmental authorities in the United States, including the FDA, and by regulatory authorities outside the United States, including the European Commission. The process of obtaining regulatory clearance or approval to market a medical diagnostic product can be costly and time-consuming, and clearance or approval for future products is never certain. Even when additional indications or uses of existing products are sought, securing clearance or approval is never certain. Delays in the receipt of, or failure to obtain clearance or approval for, future products, or new indications or uses, could result in delayed realization of product revenues and in substantial additional costs.

In addition, no assurance can be given that we will remain in compliance with applicable regulations once clearance or approval has been obtained for a product. These requirements include, among other things, regulations regarding manufacturing practices, product labeling and advertising and postmarketing reporting, including adverse event reports and field alerts due to manufacturing quality concerns. Our diagnostic product facilities and procedures and those of our suppliers are subject to ongoing regulation, including periodic inspection by the FDA and other regulatory authorities. Failure to comply with applicable rules could result in, among other things, substantial modifications to our business practices and operations; refunds, recalls or seizures of our products; a total or partial shutdown of production in one or more of our facilities while we or our suppliers remedy the alleged violation; the inability to obtain future pre-market clearances or approvals; and withdrawals or suspensions of current products from the market. Any of these events could disrupt our business and have a material adverse effect on our revenues, profitability or financial condition.

Our efforts to develop commercially successful medical diagnostic products may not succeed.

We may commit substantial efforts, funds and other resources to developing commercially successful medical diagnostic products. A high rate of failure is inherent in the development of new medical diagnostic products. There is no assurance that our efforts to develop these products will be commercially successful. Failure can occur at any point in the development process, including after significant funds have been invested.

Promising new product candidates may fail to reach the market or may have only limited commercial success because of efficacy or safety concerns, failure to achieve positive clinical outcomes, inability to obtain necessary regulatory approvals, limited scope of approved uses, excessive costs to manufacture, the failure to establish or maintain intellectual property rights, or the infringement of intellectual property rights of others. Even if we successfully develop new products or enhancements or new generations of our existing products, they may be quickly rendered obsolete by changing customer preferences or changing industry standards. Innovations may not be accepted quickly in the marketplace because of, among other things, entrenched patterns of clinical practice or uncertainty over third party reimbursement. We cannot state with certainty when or whether any of our medical diagnostic products under development will be launched, whether we will be able to develop, license or otherwise acquire products, or whether any diagnostic products will be commercially successful. Failure to launch successful new products or new indications for existing products may cause our products to become obsolete.

Our operations may be adversely impacted by the effects of natural disasters such as hurricanes and earthquakes, hostilities or acts of terrorism and other criminal activities.

Our operations may be adversely impacted by the effects of natural disasters such as hurricanes and earthquakes, hostilities or acts of terrorism or other criminal activities. Such events may result in a temporary decline in the number of patients who seek clinical testing services. In addition, such events may temporarily interrupt our ability to transport specimens, to receive materials from our suppliers or otherwise to provide our services.

Our business could be adversely impacted by CMS adoption of the new coding set for diagnoses.

CMS has adopted a new coding set for diagnosis, commonly known as ICD-10, which significantly expands the coding set for diagnoses. The new coding set is currently required to be implemented by October 1, 2013. We may be required to incur significant expense in

implementing the new coding set, and if we do not adequately implement it, our business could be adversely impacted. In addition, if as a result of the new coding set physicians fail to provide appropriate codes for desired tests, we may not be reimbursed for such tests.

Adverse results in material litigation could have an adverse financial impact and an adverse impact on our client base and reputation.

We are involved in various legal proceedings arising in the ordinary course of business including, among other things, disputes as to intellectual property, professional liability and employee-related matters, as well as inquiries from governmental agencies and Medicare or Medicaid carriers regarding billing issues. Some of the proceedings against us involve claims that are substantial in amount and could divert management s attention from operations. The proceedings also may result in substantial monetary damages, as well as damage to our reputation, and decrease the demand for our services and products, all of which could have a material adverse effect on our business. We do not have insurance or are substantially self-insured for a significant portion of any liability with respect to such claims. The ultimate outcome of the various proceedings or claims could have a material adverse effect on our financial condition, results of operations or cash flows in the period in which the impact of such matters is determined or paid.

CAUTIONARY FACTORS THAT MAY AFFECT FUTURE RESULTS

Some statements and disclosures in this document are forward-looking statements. Forward-looking statements include all statements that do not relate solely to historical or current facts and can be identified by the use of words such as may , believe , will , expect , project , estima anticipate , plan or continue. These forward-looking statements are based on our current plans and expectations and are subject to a number of risks and uncertainties that could cause our plans and expectations, including actual results, to differ materially from the forward-looking statements. Investors are cautioned not to unduly rely on such forward-looking statements when evaluating the information presented in this document. The following important factors could cause our actual financial results to differ materially from those projected, forecasted or estimated by us in forward-looking statements:

(a) Heightened competition from independent clinical testing companies, and from hospitals with respect to testing for non-patients and from physicians.

(b) Increased pricing pressure from customers and payers.

(c) A sustained decline in economic conditions, or turmoil in financial markets leading to lack of access to external capital over a sustained period of time or on reasonable terms.

(d) Impact of changes in payer mix, including any shift from fee-for-service to discounted or capitated fee arrangements.

(e) Adverse actions by government or other third-party payers, including healthcare reform that focuses on reducing healthcare costs but does not recognize the value and importance to healthcare of diagnostic testing, unilateral reduction of fee schedules payable to us, competitive bidding, and an increase in the practice of negotiating for exclusive arrangements that involve aggressively priced capitated or fee-for-service payments by health insurers or other payers.

(f) The impact upon our testing volume and collected revenue or general or administrative expenses resulting from our compliance with Medicare and Medicaid administrative policies and requirements of third party payers. These include:

(1) the requirements of Medicare carriers to provide diagnosis codes for many commonly ordered tests and the possibility that third party payers will increasingly adopt similar requirements;

(2) the policy of CMS to limit Medicare reimbursement for tests contained in automated chemistry panels to the amount that would have been paid if only the covered tests, determined on the basis of demonstrable medical necessity, had been ordered;

(3) continued inconsistent practices among the different local carriers administering Medicare;

(4) inability to obtain from patients a valid advance beneficiary notice form for tests that cannot be billed without prior receipt of the form; and

(5) increased challenges in operating as a non-contracted provider with respect to health plans.

(g) Adverse results from pending or future government investigations, lawsuits or private actions. These include, in particular, monetary damages, loss or suspension of licenses, and/or suspension or exclusion from the Medicare and Medicaid programs and/or criminal penalties.

(h) Failure to efficiently integrate acquired businesses and to manage the costs related to any such integration, or to retain key technical, professional or management personnel.

(i) Denial of CLIA certification or other licenses for any of our clinical laboratories under the CLIA standards, revocation or suspension of the right to bill the Medicare and Medicaid programs or other adverse regulatory actions by federal, state and local agencies.

(j) Changes in federal, state or local laws or regulations, including changes that result in new or increased federal or state regulation of commercial clinical laboratories or tests developed by commercial clinical laboratories, including regulation by the FDA.

(k) Inability to achieve expected benefits from our acquisitions of other businesses.

(l) Inability to achieve additional benefits from our Six Sigma and efficiency initiatives.

(m) Adverse publicity and news coverage about the clinical testing industry or us.

(n) Computer or other IT system failures that affect our ability to perform tests, report test results or properly

bill customers, including potential failures resulting from the standardization of our IT systems and other system conversions, telecommunications failures, malicious human acts (such as electronic break-ins or computer viruses) or natural disasters.

(o) Development of technologies that substantially alter the practice of clinical test medicine, including technology changes that lead to the development of more cost-effective tests such as (1) point-of-care tests that can be performed by physicians in their offices, (2) esoteric tests that can be performed by hospitals in their own laboratories or (3) home testing that can be carried out without requiring the services of clinical laboratories.

(p) Issuance of patents or other property rights to our competitors or others that could prevent, limit or interfere with our ability to develop, perform or sell our tests or operate our business.

(q) Development of tests by our competitors or others which we may not be able to license, or usage of our technology or similar technologies or our trade secrets by competitors, any of which could negatively affect our competitive position.

(r) Regulatory delay or inability to commercialize newly developed or licensed products, tests or technologies or to obtain appropriate reimbursements for such tests.

(s) Inability to obtain or maintain adequate patent and other proprietary rights protections of our products and services or to successfully enforce our proprietary rights.

(t) Impact of any national healthcare information network and the adoption of standards for health information technology interoperability that are incompatible with existing software and hardware infrastructure requiring widespread replacement of systems and/or software.

(u) Inability to promptly or properly bill for our services or to obtain appropriate payments for services that we do bill.

(v) Changes in interest rates and changes in our credit ratings from Standard & Poor s and Moody s Investor Services causing an unfavorable impact on our cost of and access to capital.

(w) Inability to hire and retain qualified personnel or the loss of the services of one or more of our key senior management personnel.

(x)

Terrorist and other criminal activities, hurricanes, earthquakes or other natural disasters, which could affect our customers, transportation or systems, or our facilities, and for which insurance may not adequately reimburse us.

(y) Difficulties and uncertainties in the discovery, development, regulatory environment and/or marketing of new products or new uses of existing products.

Item 1B. Unresolved Staff Comments

There are no unresolved SEC comments that require disclosure.

Item 2. Properties

Our executive offices are located in Madison, New Jersey. We maintain clinical testing laboratories in major metropolitan areas and elsewhere throughout the continental United States; in several instances a joint venture of which we are a partner maintains the laboratory. We also maintain offices, data centers, billing centers, call centers, an assembly center, distribution centers, and a clinical trials testing laboratory at locations throughout the United States. In addition, we maintain offices, manufacturing facilities and clinical laboratories in locations outside the United States, including in Sweden, Puerto Rico, Mexico, the United Kingdom, India and Australia. Our properties that are not owned are leased on terms and for durations that are reflective of commercial standards in the communities where these properties are located. We believe that, in general, our facilities are suitable and adequate for our current and anticipated future levels of operation and are adequately maintained. We believe that if we were unable to renew a lease on any of our facilities, we could find alternative space at competitive market rates and relocate our operations to such new location without material disruption to our business. Several of our principal facilities are highlighted below.

Location	Leased or Owned
Cypress, California	Leased
Los Angeles, California	Leased
San Juan Capistrano, California	Owned
Tampa, Florida	Owned
Atlanta, Georgia	Owned
Chicago, Illinois (2)	One owned, one leased
Baltimore, Maryland	Owned
Teterboro, New Jersey	Owned
Horsham, Pennsylvania	Leased
Norristown, Pennsylvania	Leased
Dallas, Texas	Leased
Chantilly, Virginia	Leased

Item 3. Legal Proceedings

In addition to the matters described below, in the normal course of business, we have been named, from time to time, as a defendant in various legal actions, including arbitrations, class actions and other litigation, arising in connection with our activities as a provider of diagnostic testing, information and services. These legal actions may include lawsuits alleging negligence or other similar legal claims. Certain of the actual or threatened legal actions include claims for substantial compensatory and/or punitive damages or claims for indeterminate amounts of damages, and could have an adverse impact on our client base and reputation.

The Company is also involved, from time to time, in other reviews, investigations and proceedings by governmental agencies regarding our business, including, among other matters, operational matters, certain of which may result in adverse judgments, settlements, fines, penalties, injunctions or other relief. The number of these reviews, investigations and proceedings has increased in recent years with regard to many firms in the healthcare services industry, including our Company.

We maintain various liability insurance coverages for claims that could result from providing or failing to provide clinical testing services, including inaccurate testing results and other exposures. Our insurance coverage limits our maximum exposure on individual claims; however, we are essentially self-insured for a significant portion of these claims.

The Company contests liability or the amount of damages as appropriate in each pending matter. In view of the inherent difficulty of predicting the outcome of such matters, particularly in cases where claimants seek substantial or indeterminate damages or where investigations or proceedings are in the early stages, we cannot predict with certainty the loss or range of loss, if any, related to such matters, how or if such matters will be resolved, when they ultimately will be resolved, or what the eventual settlement, fine, penalty or other relief, if any, might be. Subject to the foregoing, and except for the NID Matter which is discussed further below and in Note 14 in Notes to Consolidated Financial Statements in Part II, Item 8, we believe, based on current knowledge, that the outcome of all other pending matters will not have a material adverse effect on our consolidated financial condition, although the outcome of such matters could be material to our results of operations and cash flows in the period that such matters are determined or paid, depending on, among other things, the levels of our revenues or income for such period.

NID Matter.

NID, a test kit manufacturing subsidiary, and the Company each received a subpoena from the United States Attorney s Office for the Eastern District of New York during the fourth quarter of 2004. The subpoenas requested a wide range of business records, including documents regarding parathyroid hormone (PTH) test kits manufactured by NID and PTH testing performed by the Company. The Company has voluntarily and actively cooperated with the investigation, providing information, witnesses and business records of NID and the Company, including documents related to PTH tests and test kits, as well as other tests and test kits. In the second and third quarters of 2005, the FDA conducted an inspection of NID and issued a Form 483 listing the observations made by the FDA during the course of the inspection. NID responded to the Form 483.

During the fourth quarter of 2005, NID instituted its second voluntary product hold within a six-month period, due to quality issues, which adversely impacted the operating performance of NID. As a result, the Company evaluated a number of strategic options for NID, and on April 19, 2006, decided to cease operations at NID. Upon completion of the wind down of operations in the third quarter of 2006, the operations of NID were classified as discontinued operations. During the third quarter of 2006, the government issued two additional subpoenas, one to NID and one to the Company. The subpoenas covered various records, including records related to tests and test kits in addition to PTH.

During the third quarter of 2007, the government and the Company began settlement discussions. In the course of those discussions, the government disclosed to the Company certain of the government s legal theories regarding the amount of damages allegedly incurred by the government, which include alleged violations of civil and criminal statutes including the False Claims Act and the Food, Drug and Cosmetics Act. Violations of these statutes and related regulations could lead to a warning letter, injunction, fines or penalties, exclusion from federal healthcare programs and/or criminal prosecution, as well as claims by third parties. During the third quarter of 2008, the Company and the United States Attorney s Office reached an agreement in principle to resolve these claims. As part of the agreement, NID, which was closed in 2006, is expected to enter a guilty plea to a single count of felony misbranding. The terms of the settlement are subject to the final negotiation and execution of definitive agreements, which is expected to include a corporate integrity agreement, the approval by the United States Department of Justice and the United States Department of Health and Human Services and satisfactory resolution of related state claims. There can be no assurance, however, when or whether a settlement may be finalized, or as to its terms. If a settlement is not finalized, the Company would defend itself and NID and could incur significant costs in doing so.

The Company has established a reserve of $316 million in connection with these claims through charges reflected in discontinued operations. The reserve reflects the Company s current estimate of the expected probable loss with respect to these matters, assuming the settlement is finalized. If a settlement is not finalized, the eventual losses related to these matters could be materially different than the amount reserved and could be material to the Company s results of operations, cash flows and financial condition in the period that such matters are determined or paid.

Other Matters.

During the second quarter of 2005, the Company received a subpoena from the United States Attorney s Office for the District of New Jersey. The subpoena seeks the production of business and financial records regarding capitation and risk sharing arrangements with government and private payers for the years 1993 through 1999. Also, during the third quarter of 2005, the Company received a subpoena from the U.S. Department of Health and Human Services, Office of the Inspector General. The subpoena seeks the production of various business records including records regarding our relationship with health maintenance organizations, independent physician associations, group purchasing organizations, and preferred provider organizations relating back to as early as 1995. The Company is cooperating with the United States Attorney s Office and the Office of the Inspector General.

During the second quarter of 2006, each of the Company and its subsidiary, Specialty Laboratories, Inc. (Specialty), received a subpoena from the California Attorney General s Office. The subpoenas seek various documents including documents relating to billings to MediCal, the California Medicaid program. The subpoenas seek documents from various time frames ranging from three to ten years. During the third quarter of 2008, the Company received a request for additional information. The Company and Specialty are cooperating with the California Attorney General s Office.

In the first quarter of 2008, the United States Department of Justice informally requested records from the Company regarding AmeriPath s billing practices for flow cytometry testing panels performed on blood, bone marrow and lymph node specimens. The inquiry sought to determine whether AmeriPath may have billed for laboratory tests that were not medically necessary. The Company cooperated fully with the inquiry. In December 2008, the government declined to intervene in the underlying qui tam complaint that led to the inquiry. Following the government s declination, the qui tam relator voluntarily dismissed his complaint.

We understand that there may be pending qui tam claims brought by former employees or other whistle blowers as to which we cannot determine the extent of any potential liability. We also are aware of certain pending individual or class action lawsuits related to billing practices filed under the qui tam provisions of the civil False Claims Act and/or other federal and state statutes, regulations or other laws.

Item 4. Submission of Matters to a Vote of Security Holders

None.

PART II

Item 5. Market for Registrant s Common Stock, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is listed and traded on the New York Stock Exchange under the symbol DGX. As of February 2, 2009, we had approximately 5,700 record holders of our common stock; we believe that the number of beneficial holders of our common stock exceeds the number of record holders. The following table sets forth, for the periods indicated, the high and low sales price per share as reported on the New York Stock Exchange Consolidated Tape and dividend information.

	Common Stock Market Price		Dividends Declared
	High	Low	
2007			
First Quarter	$ 54.29	$ 48.07	$ 0.10
Second Quarter	54.75	47.98	0.10
Third Quarter	58.63	51.36	0.10
Fourth Quarter	58.23	51.91	0.10
2008			
First Quarter	$ 54.50	$ 43.65	$ 0.10
Second Quarter	51.65	45.08	0.10
Third Quarter	59.95	47.30	0.10
Fourth Quarter	52.11	38.66	0.10

We expect to fund future dividend payments with cash flows from operations, and do not expect the dividend to have a material impact on our ability to finance future growth.

The table below sets forth the information with respect to purchases made by or on behalf of the Company of its common stock during the fourth quarter of 2008.

ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in thousands)
October 1, 2008 October 31, 2008				
Share Repurchase Program (A)		N/A		$ 104,038
Employee Transactions (B)	3,246	$ 40.80	N/A	N/A
November 1, 2008 - November 30, 2008				
Share Repurchase Program (A)	2,437,297	$ 45.04	2,437,297	$ 144,257
Employee Transactions (B)	249	$ 45.14	N/A	N/A
December 1, 2008 - December 31, 2008				
Share Repurchase Program (A)	3,073,155	$ 46.93	3,073,155	$ 41(C)
Employee Transactions (B)	1,038	$ 47.49	N/A	N/A
Total				
Share Repurchase Program (A)	5,510,452	$ 46.09	5,510,452	$ 41(C)
Employee Transactions (B)	4,533	$ 42.57	N/A	N/A

(A) In November 2008, our Board of Directors expanded our common stock share repurchase authorization by an additional $150 million. Since the share repurchase program s inception in May 2003, our Board of Directors has authorized $2.3 billion of share repurchases of our common stock through December 31, 2008.

(B) Includes: (1) shares delivered or attested to in satisfaction of the exercise price and/or tax withholding obligations by holders of employee stock options (granted under the Company s Amended and Restated Employee Long-Term Incentive Plan and its Amended and Restated Director Long-Term Incentive Plan, collectively the Stock Compensation Plans) who exercised options; (2) restricted common shares withheld (under the terms of grants under the Stock Compensation Plans) to offset tax withholding obligations that occur upon vesting and release of the restricted common shares; and (3) shares withheld (under the terms of grants under the Stock Compensation Plans) to offset tax withholding obligations that occur upon the delivery of outstanding common shares underlying restricted stock units and performance share units.

(C) In January 2009, our Board of Directors authorized the Company to repurchase an additional $500 million of the Company s common stock. The share repurchase authorization has no set expiration or termination date.

Performance Graph

Set forth below is a line graph comparing the cumulative total shareholder return on Quest Diagnostics common stock since December 31, 2003, based on the market price of the Company s common stock and assuming reinvestment of dividends, with the cumulative total shareholder return of companies on the Standard & Poor s 500 Stock Index and the S&P 500 Healthcare Equipment & Services Index.

		Total Shareholder Return			*Performance Graph Values*		
Date	*Closing DGX Price(1)*	*DGX*	*S&P 500*	*S&P 500 H.C.*	*DGX*	*S&P 500*	*S&P 500 H.C.*
12/31/2004	$ 47.78	31.62%	10.88%	17.75%	$ 131.62	$ 110.88	$ 117.75
12/31/2005	$ 51.48	8.51%	4.91%	17.81%	$ 142.82	$ 116.33	$ 138.72
12/31/2006	$ 53.00	3.71%	15.79%	0.25%	$ 148.11	$ 134.70	$ 139.07
12/31/2007	$ 52.90	0.58%	5.49%	13.37%	$ 148.96	$ 142.70	$ 157.66
12/31/2008	$ 51.91	(1.08)%	(37.00)%	(37.27)%	$ 147.35	$ 89.53	$ 98.90

(1) All values are adjusted to reflect the Company s two-for-one stock split that occurred on June 20, 2005.

Item 6. Selected Financial Data

See page 39.

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

See page 41.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

See Management s Discussion and Analysis of Financial Condition and Results of Operations.

Item 8. Financial Statements and Supplementary Data

See Item 15(a)1 and Item 15(a)2.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Conclusion Regarding Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures (as defined under Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended). Based upon that evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this annual report.

Management s Report on Internal Control Over Financial Reporting

See page 57.

Changes in Internal Control

During the fourth quarter of 2008, there were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended) that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Our Code of Business Ethics applies to all employees, executive officers and directors, including our Chief Executive Officer, Chief Financial Officer and Controller. You can find our Code of Business Ethics on our internet site, *www.questdiagnostics.com*. We will post any amendments to the Code of Business Ethics, and any waivers that are required to be disclosed by the rules of either the SEC or the New York Stock Exchange, on our internet site. You can request a copy of our Code of Business Ethics, at no cost, by contacting Investor Relations, 3 Giralda Farms, Madison, New Jersey 07940 (973-520-2700).

Because our common stock is listed for trading on the New York Stock Exchange, in 2008 our Chief Executive Officer was required to make, and he made, an annual certification to the New York Stock Exchange stating that he was not aware of any violation by Quest Diagnostics of the corporate governance listing standards of the Exchange. Our Chief Executive Officer made his certification to that effect to the New York Stock Exchange on approximately June 13, 2008. In addition, we have filed, as exhibits to this Annual Report on Form 10-K, the certifications of our Chief Executive Officer and our Chief Financial Officer required under Section 302 of the Sarbanes-Oxley Act of 2002 to be filed with the SEC regarding the quality of our Company s public disclosure.

Information regarding the Company s executive officers is contained in Part I, Item 1 of this Report under Executive Officers of the Company.

Information regarding the directors and executive officers of the Company appearing in our Proxy Statement to be filed by April 28, 2009 (Proxy Statement) under the captions Matters to be Considered at the Meeting - Election of Directors, Information about our Corporate Governance Director Independence, Information about our Corporate Governance Audit and Finance Committee, and Additional Information Regarding Executive Compensation - Section 16(a) Beneficial Ownership Reporting Compliance is incorporated by reference herein.

Item 11. Executive Compensation

Information appearing in our Proxy Statement under the captions Compensation Discussion and Analysis, Additional Information Regarding Executive Compensation and Report of the Compensation Committee is incorporated by reference herein.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholders Matters

Information regarding equity compensation plans and security ownership of certain beneficial owners and management appearing in our Proxy Statement under the captions Information about our Corporate Governance Stock Ownership Information and Additional Information Regarding Executive Compensation Equity Compensation Plan Information is incorporated by reference herein.

Item 13. Certain Relationships and Related Transactions, and Director Independence

Information regarding certain relationships and related transactions appearing in our Proxy Statement under the captions Information about our Corporate Governance Related Person Transactions and Information about our Corporate Governance Director Independence is incorporated by reference herein.

Item 14. Principal Accounting Fees and Services

Information regarding principal accountant fees and services appearing in our Proxy Statement under the captions Fees and Services of PricewaterhouseCoopers LLP and Audit and Finance Committee Pre-Approval Policies and Procedures is incorporated by reference herein.

PART IV

Item 15. Exhibits, Financial Statement Schedules

(a) Documents filed as part of this Report.

1. Index to financial statements and supplementary data filed as part of this Report.

2. Financial Statement Schedule.

3. Exhibits

An exhibit index has been filed as part of this Report beginning on page E-1 and is incorporated herein by reference.

(b) Exhibits filed as part of this Report.

An exhibit index has been filed as part of this Report beginning on page E-1 and is incorporated herein by reference.

(c) None.

Signatures

Pursuant to the requirements of Sections 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on February 17, 2009.

QUEST DIAGNOSTICS INCORPORATED
(Registrant)

By: /s/ Surya N. Mohapatra, Ph.D.

Surya N. Mohapatra, Ph.D.
Chairman of the Board,
President and Chief Executive Officer

Each individual whose signature appears below constitutes and appoints Michael E. Prevoznik and William J. O Shaughnessy, Jr., and each of them singly, his or her true and lawful attorneys-in-fact and agents with full power of substitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K filed with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all the said attorneys-in-fact and agents or any of them or their or his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on February 17, 2009.

Signature	**Capacity**
/s/ Surya N. Mohapatra, Ph.D. Surya N. Mohapatra, Ph.D.	Chairman of the Board, President and Chief Executive Officer (Principal Executive Officer)
/s/ Robert A. Hagemann Robert A. Hagemann	Senior Vice President and Chief Financial Officer (Principal Financial Officer)
/s/ Thomas F. Bongiorno Thomas F. Bongiorno	Vice President, Corporate Controller and Chief Accounting Officer (Principal Accounting Officer)
/s/ John C. Baldwin, M.D. John C. Baldwin, M.D.	Director
/s/ Jenne K. Britell, Ph.D. Jenne K. Britell, Ph.D.	Director
/s/ William F. Buehler William F. Buehler	Director
/s/ Rosanne Haggerty Rosanne Haggerty	Director

/s/ Gary M. Pfeiffer	Director
Gary M. Pfeiffer	
/s/ Daniel C. Stanzione, Ph.D.	Director
Daniel C. Stanzione, Ph.D.	
/s/ Gail R. Wilensky, Ph.D.	Director
Gail R. Wilensky, Ph.D.	
/s/ John B. Ziegler	Director
John B. Ziegler	

SELECTED HISTORICAL FINANCIAL DATA OF OUR COMPANY

The following table summarizes selected historical financial data of our Company and our subsidiaries at the dates and for each of the periods presented. We derived the selected historical financial data for the years 2004 through 2008 from the audited consolidated financial statements of our Company. Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards, or SFAS, No. 123, revised 2004, Share-Based Payment (SFAS 123R), using the modified prospective approach and therefore has not restated results for prior periods. Under this approach, awards that are granted, modified or settled after January 1, 2006 will be measured and accounted for in accordance with SFAS 123R. Unvested awards that were granted prior to January 1, 2006 will continue to be accounted for in accordance SFAS No. 123, Accounting for Stock-Based Compensation, as amended by SFAS 148, Accounting for Stock-Based Compensation-Transition and Disclosure an amendment to SFAS No. 123, except that compensation cost will be recognized in the Company s results of operations. During the third quarter of 2006, the Company completed its wind down of NID, a test kit manufacturing subsidiary, and classified the operations of NID as discontinued operations. The selected historical financial data presented below has been restated to report the results of NID as discontinued operations for all periods presented. The selected historical financial data is only a summary and should be read together with the audited consolidated financial statements and related notes of our Company and management s discussion and analysis of financial condition and results of operations included elsewhere in this Annual Report on Form 10-K.

	Year Ended December 31,				
	2008	2007 (a)	2006 (b)	2005 (c)	2004
	(in thousands, except per share data)				
Operations Data:					
Net revenues	$ 7,249,447	$ 6,704,907	$ 6,268,659	$ 5,456,726	$ 5,066,986
Operating income	1,222,376 (d)	1,091,336 (e)	1,128,077 (f)	1,007,548 (g)	880,854 (h)
Income from continuing operations	632,184 (i) (j)	553,828 (k)	625,692 (l)	573,196 (m)	492,415 (n)
(Loss) / income from discontinued operations	(50,694) (o)	(213,889) (p)	(39,271) (q)	(26,919) (r)	6,780
Net income	581,490	339,939	586,421	546,277	499,195
Earnings per common share - basic: (s)					
Income from continuing operations	$ 3.25	$ 2.87	$ 3.18	$ 2.84	$ 2.42
(Loss) / income from discontinued operations	(0.26)	(1.11)	(0.20)	(0.13)	0.03
Net income	$ 2.99	$ 1.76	$ 2.98	$ 2.71	$ 2.45
Earnings per common share diluted: (s) (t)					
Income from continuing operations	$ 3.23	$ 2.84	$ 3.14	$ 2.79	$ 2.32
(Loss) / income from discontinued operations	(0.26)	(1.10)	(0.20)	(0.13)	0.03
Net income	$ 2.97	$ 1.74	$ 2.94	$ 2.66	$ 2.35
Dividends per common share (s)	$ 0.40	$ 0.40	$ 0.40	$ 0.36	$ 0.30
Balance Sheet Data (at end of year):					
Cash and cash equivalents	$ 253,946	$ 167,594	$ 149,640	$ 92,130	$ 73,302
Accounts receivable, net	832,873	881,967	774,414	732,907	649,281
Goodwill, net	5,054,926	5,220,104	3,391,046	3,197,227	2,506,950
Total assets	8,403,830	8,565,693	5,661,482	5,306,115	4,203,788
Long-term debt	3,078,089	3,377,212	1,239,105	1,255,386	724,021
Total debt	3,083,231	3,540,793	1,555,979	1,592,225	1,098,822
Total stockholders equity	3,604,896	3,324,242	3,019,171	2,762,984	2,288,651
Other Data:					
Net cash provided by operating activities	$ 1,063,049	$ 926,924	$ 951,896	$ 851,583	$ 798,780
Net cash used in investing activities	(198,883)	(1,759,193)	(414,402)	(1,079,793)	(173,700)
Net cash (used in) provided by financing activities	(777,814)	850,223	(479,984)	247,038	(706,736)
Provision for doubtful accounts	326,228	300,226	243,443	233,628	226,310
Rent expense	190,706	170,788	153,185	139,660	132,883
Capital expenditures	212,681	219,101	193,422	224,270	176,125
Depreciation and amortization	264,593	237,879	197,398	176,124	168,726

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(a) On January 31, 2007, we completed the acquisition of POCT Holding AB, (HemoCue). On May 31, 2007, we completed the acquisition of AmeriPath Group Holdings, Inc., (AmeriPath). Consolidated operating results for 2007 include the results of operations of HemoCue and AmeriPath subsequent to the closing of the applicable acquisition. See Note 3 to the Consolidated Financial Statements.

(b) On July 3, 2006, we completed the acquisition of Focus Technologies Holding Company, (Focus Diagnostics). On August 31, 2006, we completed the acquisition of Enterix Inc., (Enterix). Consolidated operating results for 2006 include the results of operations of Focus Diagnostics and Enterix subsequent to the closing of the applicable acquisition. See Note 3 to the Consolidated Financial Statements.

(c) On November 1, 2005, we completed the acquisition of Lab*One*, Inc., (LabOne). Consolidated operating results for 2005 include the results of operations of LabOne subsequent to the closing of the acquisition.

(d) For 2008, operating income includes $71 million of stock-based compensation expense recorded in accordance with SFAS 123R and $16.2 million of costs, primarily associated with workforce reductions recorded during the fourth quarter of 2008.

(e) For 2007, operating income includes $57 million of stock-based compensation expense recorded in accordance with SFAS 123R, $10.7 million of costs associated with workforce reductions in response to reduced volume levels and a pre-tax charge of $4 million related to in-process research and development expense associated with the HemoCue acquisition.

(f) For 2006, operating income includes $55 million of stock-based compensation expense recorded in accordance with SFAS 123R and $27 million of special charges, primarily associated with integration activities.

(g) For 2005, operating income includes a $6.2 million charge primarily related to forgiveness of amounts owed by patients and physicians, and related property damage as a result of hurricanes in the Gulf Coast.

(h) For 2004, operating income includes a $10.3 million charge associated with the acceleration of certain pension obligations in connection with the succession of our prior CEO.

(i) Includes an $8.9 million charge associated with the write-down of an equity investment recorded during 2008.

(j) Includes income tax benefits of $16.5 million primarily associated with favorable resolutions of certain tax contingencies in 2008.

(k) Includes a $4.0 million charge associated with the write-down of an equity investment recorded during 2007.

(l) Includes net charges of $10 million related to net investment losses recorded during 2006.

(m) Includes a $7.1 million charge associated with the write-down of an investment during 2005.

(n) Includes a $2.9 million charge during 2004 representing the write-off of deferred financing costs associated with the refinancing of our then existing bank debt and credit facility.

(o) During 2008, we recorded charges of $75 million related to the government investigation of NID. See Note 14 and Note 15 to the Consolidated Financial Statements.

(p) During 2007, we recorded charges of $241 million related to the government investigation of NID. See Note 14 and Note 15 to the Consolidated Financial Statements.

(q) During 2006, we recorded $32 million in charges related to the wind down of NID s operations. See Note 15 to the Consolidated Financial Statements.

(r) During 2005, we recorded a $16 million charge to write-off certain assets in connection with a product hold at NID.

(s) Previously reported basic and diluted earnings per share have been restated to give retroactive effect of our two-for-one stock split effected on June 20, 2005.

(t) Potentially dilutive common shares primarily include the dilutive effect of our 1¾% contingent convertible debentures issued November 26, 2001, which were redeemed principally through a conversion into common shares as of January 18, 2005, and outstanding stock options, performance share units, restricted common shares and restricted stock units granted under our Amended and Restated Employee Long-Term Incentive Plan and our Amended and Restated Director Long-Term Incentive Plan.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

Overview

The Clinical Testing Industry

Clinical testing is an essential element in the delivery of healthcare services. Physicians use laboratory tests to assist in the detection, diagnosis, evaluation, monitoring and treatment of diseases and other medical conditions.

Most laboratory tests are performed by one of three types of laboratories: commercial clinical laboratories; hospital-affiliated laboratories; and physician-office laboratories. In 2008, we estimate that hospital-affiliated laboratories accounted for approximately 60% of the market, commercial clinical laboratories approximately one-third and physician-office laboratories the balance.

Orders for laboratory testing are generated from physician offices, hospitals and employers and can be affected by a number of factors. For example, changes in the United States economy can affect the number of unemployed and uninsured, and design changes in healthcare plans can affect the number of physician office and hospital visits, and can impact the utilization of laboratory testing.

While the recent economic slow down in the United States may temporarily reduce industry growth rates, we believe the clinical testing industry will continue to grow over the long term because clinical testing is an essential healthcare service and because of the following key trends:

- the growing and aging population;
- continuing research and development in the area of genomics (the study of DNA, genes and chromosomes) and proteomics (the analysis of individual proteins and collections of proteins), which is expected to yield new, more sophisticated and specialized diagnostic tests;
- increasing recognition by consumers and payers of the value of laboratory testing as a means to improve health and reduce the overall cost of healthcare through early detection and prevention;
- increasing affordability of, and access to, tests due to advances in technology and cost efficiencies; and
- the growing demand for healthcare services in emerging markets and global demographic changes.

The diagnostic testing industry is subject to seasonal fluctuations in operating results and cash flows. Typically, testing volume declines during the summer months, year-end holiday periods and other major holidays, reducing net revenues and operating cash flows below annual averages. Testing volume is also subject to declines due to severe weather or other events, which can deter patients from having testing performed and which can vary in duration and severity from year to year.

Reimbursement for Services

Payments for clinical testing services are made by physicians, hospitals, employers, healthcare plans, patients and the government. Physicians, hospitals and employers are typically billed on a fee-for-service basis based on negotiated fee schedules. Fees billed to healthcare plans and patients are based on the laboratory s patient fee schedule, subject to any limitations on fees negotiated with the healthcare plans or with physicians on behalf of their patients. Medicare and Medicaid reimbursements are based on fee schedules set by governmental authorities.

Government payers, such as Medicare and Medicaid, as well as healthcare plans and larger employers, have taken steps and may continue to take steps to control the cost, utilization and delivery of healthcare services, including clinical testing services. Despite the added cost and complexity of participating in the Medicare and Medicaid programs, we continue to participate in such programs because we believe that our other business may depend, in part, on continued participation in these programs, since certain customers may want a single laboratory capable of performing all of their clinical testing services, regardless of who pays for such services.

Healthcare plans, which typically negotiate directly or indirectly on behalf of their members, represent approximately one-half of our clinical testing volumes and one-half of our net revenues from our clinical testing business. Larger healthcare plans typically prefer to use large commercial clinical laboratories because they can provide services to their members on a national or regional basis. In addition, larger clinical laboratories are better able to achieve the low-cost structures necessary to profitably service the members of large healthcare plans and can provide test utilization data across various products in a consistent format. In certain markets, such as California, healthcare plans may delegate their covered members to independent physician associations (IPAs), which in turn negotiate with laboratories for clinical testing services on

behalf of their members.

The trend of consolidation among physicians, hospitals, employers, healthcare plans, pharmaceutical companies and other intermediaries has continued, resulting in fewer but larger customers and payers with significant bargaining power to negotiate fee arrangements with healthcare providers, including clinical laboratories. Healthcare plans often require that clinical testing service providers accept discounted fee structures or assume all or a portion of the utilization risk associated with providing testing services to their members enrolled in highly-restricted plans through capitated payment arrangements. Under these capitated payment arrangements, we and the healthcare plans agree to a predetermined monthly reimbursement rate for each member enrolled in the healthcare plan s restricted plan, generally regardless of the number or cost of services provided by us. Our cost to perform work reimbursed under capitated payment arrangements is not materially different from our cost to perform work reimbursed under other arrangements with healthcare plans. Since average reimbursement rates under capitated payment arrangements are typically less than our overall average reimbursement rate, the testing services reimbursed under capitated payment arrangements are generally less profitable. In 2008, we derived approximately 14% of our testing volume and 5% of our net revenues from capitated payment arrangements.

Most healthcare plans also offer programs such as preferred provider organizations (PPOs) and consumer driven health plans that offer a greater choice of healthcare providers. Pricing for these programs is typically negotiated on a fee-for-service basis, which generally results in higher revenue per requisition than under capitation arrangements. Most of our agreements with major healthcare plans are non-exclusive arrangements. As a result, under these non-exclusive arrangements, physicians and patients have more freedom of choice in selecting laboratories, and laboratories are likely to compete more on the basis of service and quality than they may otherwise. If consumer driven plans and PPO plans continue to increase in popularity, it will be increasingly important for healthcare providers to differentiate themselves based on quality, service and convenience to avoid competing on price alone.

Despite the general trend of increased choice for patients in selecting a healthcare provider, recent experience indicates that some healthcare plans may actively seek to limit the choice of patients and physicians if they feel it will give them increased leverage to negotiate lower fees, by consolidating services with a single or limited network of contracted providers. Historically, healthcare plans, which had limited their network of laboratory service providers, encouraged their members, and sometimes offered incentives, to utilize only contracted providers. Patients who use a non-contracted provider may have a higher co-insurance responsibility, which may result in physicians referring testing to contracted providers to minimize the expense to their patients. In cases where members choose to use a non-contracted provider due to service quality or convenience, the non-contracted provider would be reimbursed at rates considered reasonable and customary. Contracted rates are generally lower than reasonable and customary rates because of the potential for greater volume as a contracted provider. A non-contracted laboratory service provider with quality and service preferred by physicians and patients to that of contracted providers, could potentially realize greater profits than if it was a contracted provider, provided that physicians and patients continue to have choice in selecting their provider, and any potential additional cost to the patient of using a non-contracted provider is not considered prohibitive. Physicians requiring testing for patients are the primary referral source of our clinical testing volume, and often refer work to us as a non-contracted provider.

We expect that reimbursements for the diagnostic testing industry will continue to remain under pressure. Today, the federal and many state governments face serious budget deficits and healthcare spending is subject to reductions, and efforts to reduce reimbursements and stringent cost controls by government and other payers for existing tests may continue. However, we believe that as new tests are developed which either improve on the effectiveness of existing tests or provide new diagnostic capabilities, government and other payers will add these tests as covered services, because of the importance of laboratory testing in assessing and managing the health of patients. We continue to emphasize the importance and the high value of laboratory testing with healthcare plans and government payers at the federal and state level.

Our Company

Quest Diagnostics is the world s leading provider of diagnostic testing, information and services, providing insights that enable patients, physicians and others to make decisions to improve health. Quest Diagnostics, with a leading position in most of its domestic geographic markets and service offerings, is well positioned to benefit from the long-term growth expected in the industry. Over 90% of our revenues are derived from clinical testing with the balance derived from insurer services, clinical trials testing, diagnostic products and healthcare information technology. Clinical testing is generally categorized as clinical laboratory testing and anatomic pathology services. Clinical laboratory testing is performed on blood and body fluids, such as urine. Anatomic pathology services are performed on tissues, such as biopsies, and other samples, such as human cells. With the acquisition of AmeriPath Group Holdings, Inc. (AmeriPath) in May 2007, we have become the world s premier cancer diagnostics company, focused on anatomic pathology including dermatopathology and molecular diagnostics and are now able to provide interpretive consultation through the largest medical and scientific staff in the industry, with approximately 900 M.D.s and Ph.D.s primarily located in the United

States. In addition, we are the leading provider of gene-based testing and other esoteric testing, risk assessment services for the life insurance industry and testing for drugs-of-abuse. We are also a leading provider of testing for clinical trials. The Company s diagnostics products business, which includes the operations of HemoCue, Enterix and certain of Focus Diagnostics operations, manufactures and markets diagnostic test kits and specialized point-of-care testing. Through our MedPlus subsidiary, we empower healthcare organizations and clinicians with state-of-the-art information technology solutions that can improve patient care and medical practice.

We have established operations in Gurgaon, India, where we will offer many of our services. The diagnostic testing business in India is poised for rapid expansion. We see significant opportunities for us to strengthen the delivery of healthcare services in India utilizing our quality diagnostics and technology expertise.

Six Sigma and Standardization Initiatives/Efforts to Improve Operating Efficiency

The diagnostic testing industry is labor intensive. Employee compensation and benefits constitute approximately one-half of our total costs and expenses. Cost of services consists principally of costs for obtaining, transporting and testing specimens. Selling, general and administrative expenses consist principally of the costs associated with our sales and marketing efforts, billing operations (including bad debt expense), and general management and administrative support. In addition, performing diagnostic testing involves significant fixed costs for facilities and other infrastructure required to obtain, transport and test specimens. Therefore, relatively small changes in volume can have a significant impact on profitability in the short-term.

A large portion of our costs are fixed, making it more challenging to fully mitigate the profit impact of lost volume in the short term. In July 2007, we announced a program to adjust our cost structure while maintaining and, in some cases improving, service levels. During 2008, we continued to take actions which have enabled us to improve margins as a percentage of revenues over the course of the year and achieve a level which exceeded that of the prior year. As we exited 2008, we estimate that our program has resulted in over $300 million of annualized cost reductions, and we expect that our program will result in $500 million of annualized cost reductions as we exit 2009.

We intend to become recognized as the quality leader in the healthcare services industry through utilizing the Six Sigma approach and Lean Six Sigma principles. Six Sigma is a management approach that enhances quality and requires a thorough understanding of customer needs and experience, root cause analysis, process improvements and rigorous tracking and measuring of key metrics. Lean Six Sigma streamlines processes and eliminates waste. We utilize the Six Sigma approach and Lean Six Sigma principles to increase the efficiency of our operations and to reduce operating cost. We have utilized Six Sigma to implement the initiatives which are part of our cost reduction program and provide a better customer experience. These initiatives relate to standardizing our operations and processes, and adopting identified company best practices. One of these key initiatives is to deploy Lean Six Sigma in our laboratories to realize productivity gains. Additionally, we expect to realize efficiencies in other areas by better aligning our service capacity with patient and sample flows. We are driving more of our purchasing through master contracts to take better advantage of our scale. We are expanding the use of customer connectivity which reduces costs in specimen data entry and billing, and helps lower our bad debt. We are improving the efficiency of our logistics routes using advanced route optimization tools and we have streamlined our management structure and administrative functions to improve efficiency and increase focus. As additional detailed plans to implement these opportunities are approved and executed, some will result in charges to earnings associated with the implementation. These charges may be material to the results of operations and cash flows in the periods recorded or paid.

Recent Acquisitions

The clinical testing industry in the United States remains fragmented and highly competitive. Our growth will be comprised of a combination of organic and acquired growth. 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 United States diagnostic testing industry and the differentiated services we offer to our customers will enable us to grow organically, we believe there will continue to be opportunities to grow beyond our current principal business of offering clinical testing in the United States. Technology is enabling testing to be performed closer to the patient, whether in the physician s office or at the hospital bedside, in the form of point-of-care testing. Given that physicians and hospitals are primary sources for both point-of-care testing and laboratory performed tests, we believe providing both services will strengthen our relationships with customers and accelerate our growth.

Additionally, diagnostic testing in international markets, particularly developing countries, is highly fragmented and less mature. Continued expansion into point-of-care testing and international markets will diversify our revenue base, and add businesses in markets which are growing faster and are more profitable than our principal business of United States based clinical testing.

Acquisition of AmeriPath

On May 31, 2007, we completed the acquisition of AmeriPath, in an all-cash transaction valued at approximately $2 billion, including approximately $780 million of assumed debt and related accrued interest. AmeriPath is a leading provider of anatomic pathology, including dermatopathology, and esoteric testing which generated annual revenues of approximately $800 million.

Through the acquisition, we acquired all of AmeriPath s operations. AmeriPath, with its team of approximately 400 board certified pathologists, operates 40 outpatient anatomic pathology testing locations and provides inpatient anatomic pathology and medical director services for approximately 200 hospitals throughout the United States. We financed the all-cash purchase price and related transaction costs, together with the repayment of approximately $780 million of principal and related accrued interest representing substantially all of AmeriPath s debt, as well as the refinancing of the $450 million term loan used to finance the acquisition of HemoCue, with $1.6 billion of borrowings under a five-year term loan facility, $780 million of borrowings under a one-year bridge loan, and cash on-hand. In June 2007, we completed an $800 million senior notes offering. The net proceeds of the senior notes offering were used to repay the $780 million bridge loan. The acquisition was accounted for under the purchase method of accounting.

Acquisition of HemoCue

On January 31, 2007, we acquired HemoCue, a Sweden-based company specializing in point-of-care testing, in an all-cash transaction valued at approximately $450 million, including $113 million of assumed debt of HemoCue. The transaction was financed through an interim credit facility, which was refinanced during the second quarter of 2007 in connection with the financing of the AmeriPath acquisition.

HemoCue is the leading international provider in point-of-care testing for hemoglobin, with a growing share in professional glucose and microalbumin testing.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions and select accounting policies that affect our reported financial results and the disclosure of contingent assets and liabilities.

While many operational aspects of our business are subject to complex federal, state and local regulations, the accounting for most of our business is generally straightforward with net revenues primarily recognized upon completion of the testing process. Our revenues are primarily comprised of a high volume of relatively low dollar transactions, and about one-half of our total costs and expenses consist of employee compensation and benefits. Due to the nature of our business, several of our accounting policies involve significant estimates and judgments:

- revenues and accounts receivable associated with clinical testing;
- reserves for general and professional liability claims;
- reserves for other legal proceedings;
- accounting for and recoverability of goodwill; and
- accounting for stock-based compensation expense.

Revenues and accounts receivable associated with clinical testing

The process for estimating the ultimate collection of receivables associated with our clinical testing business involves significant assumptions and judgments. Billings for services reimbursed by third-party payers, including Medicare and Medicaid, are recorded as revenues net of allowances for differences between amounts billed and the estimated receipts from such payers. Adjustments to the estimated receipts, based on final settlement with the third-party payers, are recorded upon settlement as an adjustment to net revenues.

We have a standardized approach to estimate and review the collectibility of our receivables based on a number of factors, including the period they have been outstanding. Historical collection and payer reimbursement experience is an integral part of the estimation process related to allowances for doubtful accounts. In addition, we regularly assess the state of our billing operations in order to identify issues, which may impact the collectibility of receivables or allowance estimates. We believe that the collectibility of our receivables is directly linked to the quality of our billing processes, most notably those related to obtaining the correct information in order to bill effectively for the services we provide. As such, we have implemented best practices to reduce the number of requisitions that we receive from healthcare providers with missing or incorrect billing information. Revisions to the allowances for doubtful accounts estimates are recorded as an adjustment to bad debt expense within selling, general and administrative expenses. We believe that our

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collection and allowance estimation processes, along with our close monitoring of our billing operations, help to reduce the risk associated with material revisions to reserve estimates. Less than 5% of our net accounts receivable as of December 31, 2008 were outstanding more than 150 days.

Healthcare insurers

Healthcare insurers reimburse us for approximately one-half of our net revenues. Reimbursements from healthcare insurers are based on negotiated fee-for-service schedules and on capitated payment rates.

Receivables due from healthcare insurers represent approximately 28% of our net accounts receivable. Substantially all of the accounts receivable due from healthcare insurers represent amounts billed under negotiated fee-for-service arrangements. We utilize a standard approach to establish allowances for doubtful accounts for such receivables, which considers the aging of the receivables and results in increased allowance requirements as the aging of the related receivables increases. Our approach also considers historical collection experience and other factors. Collection of such receivables is normally a function of providing complete and correct billing information to the healthcare insurers within the various filing deadlines. For healthcare insurers, collection typically occurs within 30 to 60 days of billing. Provided healthcare insurers have been billed accurately with complete information prior to the established filing deadline, there has historically been little to no collection risk. If there has been a delay in billing, we determine if the amounts in question will likely go past the filing deadline, and if so, we will reserve accordingly for the billing.

Approximately 5% of our net revenues are reimbursed under capitated payment arrangements in which case the healthcare insurers typically reimburse us in the same month services are performed, essentially giving rise to no outstanding accounts receivable at month-end. If any capitated payments are not received on a timely basis, we determine the cause and make a separate determination as to whether or not the collection of the amount from the healthcare insurer is at risk and if so, would reserve accordingly.

Government payers

Payments for clinical testing services made by the government are based on fee schedules set by governmental authorities. Receivables due from government payers under the Medicare and Medicaid programs represent approximately 15% of our net accounts receivable. Collection of such receivables is normally a function of providing the complete and correct billing information within the various filing deadlines. Collection typically occurs within 30 days of billing. Our processes for billing, collecting and estimating uncollectible amounts for receivables due from government payers, as well as the risk of non-collection, are substantially the same as those noted above for healthcare insurers under negotiated fee-for-service arrangements.

Client payers

Client payers include physicians, hospitals, employers and other commercial laboratories, and are billed based on a negotiated fee schedule. Receivables due from client payers represent approximately 34% of our net accounts receivable. Credit risk and ability to pay are more of a consideration for these payers than healthcare insurers and government payers. We utilize a standard approach to establish allowances for doubtful accounts for such receivables, which considers the aging of the receivables and results in increased allowance requirements as the aging of the related receivables increase. Our approach also considers specific account reviews, historical collection experience and other factors.

Patient receivables

Patients are billed based on established patient fee schedules, subject to any limitations on fees negotiated with healthcare insurers or physicians on behalf of the patient. Receivables due from patients represent approximately 23% of our net accounts receivable. Collection of receivables due from patients is subject to credit risk and ability of the patients to pay. We utilize a standard approach to establish allowances for doubtful accounts for such receivables, which considers the aging of the receivables and results in increased allowance requirements as the aging of the related receivables increases. Our approach also considers historical collection experience and other factors. Patient receivables are generally fully reserved for when the related billing reaches 210 days outstanding. Balances are automatically written off when they are sent to collection agencies. Reserves are adjusted for estimated recoveries of amounts sent to collection agencies based on historical collection experience, which is regularly monitored.

Reserves for general and professional liability claims

As a general matter, providers of clinical testing services may be subject to lawsuits alleging negligence or other similar legal claims. These suits could involve claims for substantial damages. Any professional liability litigation could also have an adverse impact on our client base and reputation. We maintain various liability insurance coverages for claims that could result from providing or failing to provide clinical testing services including inaccurate testing results

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and other exposures. Our insurance coverage limits our maximum exposure on individual claims; however, we are essentially self-insured for a significant portion of these claims. While the basis for claims reserves considers actuarially determined losses based upon our historical and projected loss experience, the process of analyzing, assessing and establishing reserve estimates relative to these types of claims involves a high degree of judgment. Changes in the facts and circumstances associated with claims could have a material impact on our results of operations, principally costs of services, and cash flows in the period that reserve estimates are revised or paid. Although we believe that our present insurance coverage and reserves are sufficient to cover currently estimated exposures, it is possible that we may incur liabilities in excess of our insurance coverage or recorded reserves.

Reserves for other legal proceedings

Our business is subject to extensive and frequently changing federal, state and local laws and regulations. In addition, we are aware of certain pending lawsuits related to billing practices filed under the qui tam provisions of the False Claims Act and other federal and state statutes. See Notes 14 and 15 to the Consolidated Financial Statements for a discussion of the various legal proceedings that involve the Company. We have a comprehensive compliance program that is intended to ensure the strict implementation and observance of all applicable laws, regulations and Company policies. Management periodically reports to the Quality, Safety & Compliance Committee of our Board of Directors regarding compliance operations. As an integral part of our compliance program, we investigate all reported or suspected failures to comply with federal and state healthcare reimbursement requirements. Any non-compliance that results in Medicare or Medicaid overpayments is reported to the government and reimbursed by us. As a result of these efforts, we have periodically identified and reported overpayments. Upon becoming aware of potential overpayments, we consider all available facts and circumstances to estimate and record the amounts to be reimbursed. While we have reimbursed these overpayments and have taken corrective action where appropriate, the government may not in each instance accept these actions as sufficient.

The process of analyzing, assessing and establishing reserve estimates relative to legal proceedings involves a high degree of judgment. Management has established reserves for legal proceedings in accordance with generally accepted accounting principles. Changes in facts and circumstances related to such proceedings could lead to significant revisions to reserve estimates for such matters and could have a material impact on our results of operations, cash flows and financial condition in the period that reserve estimates are revised or paid.

Accounting for and recoverability of goodwill

Goodwill is our single largest asset. We evaluate the recoverability and measure the potential impairment of our goodwill under Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets. The annual impairment test is a two-step process that begins with the estimation of the fair value of the reporting unit. The first step screens for potential impairment and the second step measures the amount of the impairment, if any. Our estimate of fair value considers publicly available information regarding the market capitalization of our Company, as well as (i) the financial projections and future prospects of our business, including its growth opportunities and likely operational improvements, and (ii) comparable sales prices, if available. As part of the first step to assess potential impairment, we compare our estimate of fair value for the reporting unit to the book value of the reporting unit. If the book value is greater than our estimate of fair value, we would then proceed to the second step to measure the impairment, if any. The second step compares the implied fair value of goodwill with its carrying value. The implied fair value is determined by allocating the fair value of the reporting unit to all of the assets and liabilities of that unit as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the purchase price paid to acquire the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. If the carrying amount of the reporting unit s goodwill is greater than its implied fair value, an impairment loss will be recognized in the amount of the excess. We believe our estimation methods are reasonable and reflect common valuation practices.

On a quarterly basis, we perform a review of our business to determine if events or changes in circumstances have occurred which could have a material adverse effect on the fair value of the Company and its goodwill. If such events or changes in circumstances were deemed to have occurred, we would perform an impairment test of goodwill as of the end of the quarter, consistent with the annual impairment test performed at the end of our fiscal year on December 31st, and record any noted impairment loss.

Accounting for stock-based compensation expense

Effective January 1, 2006, we adopted SFAS No. 123, revised 2004, Share-Based Payment (SFAS 123R), using the modified prospective approach and therefore have not restated results for prior periods. Pursuant to the provisions of SFAS 123R, we record stock-based compensation as a charge to earnings net of the estimated impact of forfeited awards. As such, we recognize stock-based compensation cost only for those stock-based awards that are estimated to ultimately vest over their requisite service period, based on the vesting provisions of the individual grants.

The process of estimating the fair value of stock-based compensation awards and recognizing stock-based compensation cost over their requisite service periods involves significant assumptions and judgments. We estimate the fair value of stock option awards on the date of grant using a lattice-based option-valuation model which requires management to make certain assumptions regarding: (i) the expected volatility in the market price of the Company s common stock; (ii) dividend yield; (iii) risk-free interest rates; and (iv) the period of time employees are expected to hold the award prior to exercise (referred to as the expected holding period). The expected volatility under the lattice-based option-valuation model is based on the current and historical implied volatilities from traded options of our common stock. The dividend yield is based on the approved annual dividend rate in effect and current market price of the underlying common stock at the time of grant. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for bonds with maturities ranging from one month to seven years. The expected holding period of the awards granted is estimated using the historical exercise behavior of employees. In addition, SFAS 123R requires us to estimate the expected impact of forfeited awards and recognize stock-based compensation cost only for those awards expected to vest. We use historical experience to estimate projected forfeitures. If actual forfeiture rates are materially different from our estimates, stock-based compensation expense could be significantly different from what we have recorded in the current period. We periodically review actual forfeiture experience and revise our estimates, as considered necessary. The cumulative effect on current and prior periods of a change in the estimated forfeiture rate is recognized as compensation cost in earnings in the period of the revision.

Finally, the terms of our performance share unit grants allow the recipients of such awards to earn a variable number of shares based on the achievement of the performance goals specified in the awards. For performance share unit awards granted prior to 2008, the actual amount of any stock award earned is based on the Company s earnings per share growth as measured in accordance with its Amended and Restated Employee Long-Term Incentive Plan for the performance period compared to that of a peer group of companies. Beginning with performance share unit awards granted in 2008, the performance measure for these awards will be based on the cumulative annual growth rate of the Company s earnings per share from continuing operations over a three year period. Stock-based compensation expense associated with performance share units is recognized based on management s best estimates of the achievement of the performance goals specified in such awards and the resulting number of shares that will be earned. If the actual number of performance share units earned is different from our estimates, stock-based compensation could be significantly different from what we have recorded in the current period. We periodically obtain and review publicly available financial information for the members of the peer group and compare that to actual and estimated future performance of the Company, including historical earnings per share growth as well as published estimates of projected earnings per share growth. This information is used to evaluate our progress towards achieving the performance criteria and our estimate of the number of performance share units expected to be earned at the end of the performance period. The cumulative effect on current and prior periods of a change in the estimated number of performance share units expected to be earned is recognized as compensation cost in earnings in the period of the revision. While the assumptions used to calculate and account for stock-based compensation awards represent management s best estimates, these estimates involve inherent uncertainties and the application of management s judgment. As a result, if revisions are made to our assumptions and estimates, our stock-based compensation expense could vary significantly from period to period. In addition, the number of awards made under our equity compensation plans, changes in the design of those plans, the price of our shares and the performance of our Company can all cause stock-based compensation expense to vary from period to period.

Results of Operations

Our clinical testing business currently represents our one reportable business segment. The clinical testing business for each of the three years in the period ended December 31, 2008 accounted for more than 90% of net revenues from continuing operations. Our other operating segments consist of our risk assessment services business, our clinical trials testing business, our healthcare information technology business, MedPlus, and our diagnostic products business. On April 19, 2006, we decided to discontinue the operations of a test kit manufacturing subsidiary, NID. During the third quarter of 2006, we completed the wind down of NID and classified the operations of NID as discontinued operations for all periods presented. Our business segment information is disclosed in Note 16 to the Consolidated Financial Statements.

Year Ended December 31, 2008 Compared with Year Ended December 31, 2007

Continuing Operations

Income from continuing operations for the year ended December 31, 2008 was $632 million, or $3.23 per diluted share, compared to $554 million, or $2.84 per diluted share, in 2007. The increase in income from continuing operations was principally driven by revenue growth and actions we have taken to reduce our cost structure.

Results for the year ended December 31, 2008 include charges totaling $25.1 million, or $0.08 per diluted share consisting of: a third quarter charge of $8.9 million, or $0.03 per diluted share, associated with the write-down of an equity investment; and a fourth quarter charge of $16.2 million, or $0.05 per diluted share, principally associated with workforce reductions. These charges were offset in part by favorable resolutions of certain tax contingencies in 2008, which increased diluted earnings per share by $0.08.

In addition, for 2008 we estimate the impact of hurricanes in the third quarter of 2008 reduced the increase in operating income for the year ended December 31, 2008 by approximately $8 million or $0.02 per diluted share, compared to the prior year.

During the first quarter of 2007, we became a non-contracted provider to United Healthcare Group Inc., (UNH). As a result of the change in status, our revenues and earnings were significantly impacted for the first quarter and full year 2007. However, the ongoing profit impact was successfully mitigated by the end of 2007 as a result of our actions to reduce costs, and higher reimbursement for the testing we continued to perform for UNH members as a non-contracted provider.

Results for the year ended December 31, 2007 include first quarter pre-tax charges of $10.7 million, or $0.03 per diluted share, associated with workforce reductions in response to reduced volume levels, and a first quarter pre-tax charge of $4.0 million, or $0.01 per diluted share, related to in-process research and development expense associated with the HemoCue acquisition.

Net Revenues

Net revenues for the year ended December 31, 2008 grew by 8.1% over the prior year level to $7.2 billion, with the carry-over impact from the 2007 acquisition of AmeriPath contributing approximately 5.0% to revenue growth in 2008.

For 2008, revenues of our clinical testing business, which accounts for over 90% of our net revenues, grew 8.3% above the prior year level, with AmeriPath contributing 5.5% growth. Volume, measured by the number of requisitions, increased 2.7% for the year ended December 31, 2008, with 2.4% due to the impact of the AmeriPath acquisition. Our pre-employment drug testing volume, which accounted for approximately 7% of our total volume in 2008, declined approximately 11% and reduced consolidated volume by approximately 1%. We believe the volume decrease in pre-employment drug testing is principally due to slower hiring by employers served by this business. Revenue per requisition increased 5.5% for the year ended December 31, 2008, with AmeriPath contributing 2.9% to the improvement. The balance of the increase was primarily driven by a positive mix, partially offset by price reductions on various health plan contracts.

Our businesses other than clinical testing accounted for approximately 9% of our net revenues in 2008. These businesses include our risk assessment services business, our clinical trials testing business, our healthcare information technology business, MedPlus, and our diagnostic products business. The revenues for these businesses as a group grew 6% for the year ended December 31, 2008 with the increase primarily driven by our healthcare information technology and point-of-care businesses.

Operating Costs and Expenses

Total operating costs and expenses for the year ended December 31, 2008 increased $414 million from the prior year period. These increases were primarily due to the full year effect of costs associated with the acquired operations of AmeriPath, and increased costs associated with annual compensation adjustments, partially offset by actions taken to improve our operating efficiency and reduce the size of our workforce. Results for the year ended December 31, 2008 also include fourth quarter charges of $16.2 million primarily associated with workforce reductions ($7.7 million recorded in costs of services and $8.5 million included in selling, general and administrative).

Results for the year ended December 31, 2007 reflect first quarter costs of $10.7 million associated with workforce reductions ($3.9 million included in cost of services and $6.8 million included in selling, general and administrative), $4 million of in-process research and development costs associated with the acquisition of HemoCue, which was recorded in other operating (income) expense, net , and costs associated with efforts to retain business and clarify for patients, physicians and employers misinformation regarding the UNH contract change.

Cost of services, which includes the costs of obtaining, transporting and testing specimens, was 58.7% of net revenues for the year ended December 31, 2008, compared to 59.2% of net revenues in 2007. The improvement over the prior year reflects actions taken to reduce our cost structure and higher revenue per requisition.

Selling, general and administrative expenses, which include the costs of the sales force, billing operations, bad debt expense, and general management and administrative support, were 24.0% of net revenues for the year ended December 31, 2008, compared to 24.1% in the prior year period. The improvement was primarily due to actions taken to reduce our cost structure and higher revenue per requisition, partially offset by the full year impact of the acquired operations of AmeriPath and costs associated with workforce reductions.

Selling, general and administrative expenses for the year ended December 31, 2007 included costs associated with workforce reductions and costs associated with efforts to retain business and clarify for patients, physicians and employers misinformation regarding the UNH contract change.

For the year ended December 31, 2008, bad debt expense was 4.5% of net revenues similar to 2007. For 2008, the full year inclusion of AmeriPath, which carries a higher bad debt rate than the rest of our business, primarily due to its revenue and customer mix, increased the consolidated bad debt rate by approximately half a percent for 2008. The impact was principally offset by progress in our billing and collection processes, resulting in improvements in bad debt, days sales outstanding and the cost of our billing operation. With our disciplined approach, we expect to see continued strong performance in our billing and collection metrics, despite a slowing economy.

Amortization of intangible assets for the year ended December 31, 2008 increased $9.4 million over the prior year period. This increase was primarily due to the amortization of intangible assets acquired in conjunction with the acquisition of AmeriPath.

Other operating (income) expense, net represents miscellaneous income and expense items related to operating activities, including gains and losses associated with the disposal of operating assets and provisions for restructurings and other special charges. For the year ended December 31, 2007, other operating (income) expense, net includes a $4.0 million first quarter charge related to in-process research and development expense recorded in connection with the acquisition of HemoCue.

Operating Income

Operating income for the year ended December 31, 2008 was $1.2 billion, or 16.9% of net revenues, compared to $1.1 billion, or 16.3% of net revenues, in the prior year period. The increase in operating income, as a percentage of net revenues, was primarily due to revenue growth and the actions we have taken to reduce our cost structure, partially offset by the full year impact of the acquired operations of AmeriPath. In addition, we estimate the impact of hurricanes in the third quarter of 2008 reduced the increase in operating income for the year ended December 31, 2008 by approximately $8 million, compared to the prior year.

In addition, the operating income percentage for the year ended December 31, 2008, reflects the impact of a fourth quarter charge of $16.2 million, principally associated with workforce reductions and the impact of the various items which affected cost of services and selling, general and administrative expenses as a percentage of net revenues.

Other (Income) Expense

Other expense, net represents miscellaneous income and expense items related to non-operating activities such as gains and losses associated with investments and other non-operating assets. For the year ended December 31, 2008, other expense, net includes a third quarter charge of $8.9 million associated with the write-down of an equity investment and losses of $9.9 million associated with investments held in a trust pursuant to our supplemental deferred compensation plan. For the year ended December 31, 2007, other expense, net includes a $4 million charge related to the write-down of an investment.

Income Tax Expense

The effective income tax rate for the year ended December 31, 2008 decreased 1.3 percentage points, compared to the prior year period. This decrease was primarily due to the favorable resolution of certain tax contingencies in 2008.

Discontinued Operations

During the third quarter of 2008, the Company and NID, a former test kit manufacturing subsidiary of the Company, reached an agreement in principle with the United States Attorney s Office to settle the previously disclosed federal government investigation involving NID and the Company regarding NID test kits and tests performed using those test kits.

The agreement in principle provides for a comprehensive settlement of federal claims. As part of the agreement, NID, which was closed in 2006, is expected to enter a guilty plea to a single count of felony misbranding. The terms of the settlement are subject to the final negotiation and execution of definitive agreements, which is expected to include a corporate integrity agreement, and the approval by the United States Department of Justice and the United States Department of Health and Human Services and satisfactory resolution of related state claims. There can be no assurance, however, when or whether a settlement may be finalized, or as to its terms. If a settlement is not finalized, the Company would defend itself and NID and could incur significant costs in doing so.

As a result of the agreement in principle in 2008, the Company recorded charges of $75 million in discontinued operations to increase its reserve for the settlement and related matters. As of December 31, 2008, the total reserve was $316 million. The Company has recorded deferred tax benefits of $58 million on the reserve, reflecting the Company s

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current estimate of the portion of the reserve expected to be deductible for tax purposes. The reserve reflects the Company s current estimate of the expected probable loss with respect to these matters, assuming the settlement is finalized. If a settlement is not finalized, the eventual losses related to these matters could be materially different than the amount reserved and could be material to the Company s results of operations, cash flows and financial condition in the period that such matters are determined or paid.

Loss from discontinued operations, net of taxes, for the year ended December 31, 2008 was $51 million, or $0.26 per diluted share, compared to $214 million, or $1.10 per diluted share in 2007. Results for the year ended December 31, 2008 and 2007 reflect charges of $75 million and $241 million, respectively, to reserve for the settlement and related matters in connection with various government claims, which is more fully described in Note 14 and Note 15 to the Consolidated Financial Statements.

Year Ended December 31, 2007 Compared with Year Ended December 31, 2006

Continuing Operations

Income from continuing operations for the year ended December 31, 2007 was $554 million, or $2.84 per diluted share, compared to $626 million, or $3.14 per diluted share in 2006. The decrease in income from continuing operations was principally due to the impact of the change in contract status with UNH. However, we successfully mitigated the ongoing impact during the third quarter of 2007 as a result of actions taken to reduce costs, and higher reimbursement for the testing we continue to perform for UNH members. During the second half of the year our profits, before considering the acquisition of AmeriPath, exceeded those of the prior year, when we were a contracted provider to UNH. The acquisition of AmeriPath, which was completed in May 2007, also served to reduce income from continuing operations compared to the prior year. We expect the acquisition of AmeriPath to improve our revenue growth and earnings once the anticipated growth opportunities and cost synergies associated with the acquisition are realized. Results for the year ended December 31, 2007 include first quarter pre-tax charges of $10.7 million, or $0.03 per diluted share, associated with workforce reductions in response to reduced volume levels and $4.0 million, or $0.01 per diluted share, related to in-process research and development expense associated with the HemoCue acquisition.

Net Revenues

Net revenues for the year ended December 31, 2007 grew by 7.0% over the prior year level to $6.7 billion. The acquisition of AmeriPath contributed approximately 8% to revenue growth. Our acquisitions of Focus Diagnostics, Enterix and HemoCue contributed approximately 1.7% to revenue growth. We estimate the impact of our change in status with UNH reduced revenue growth by approximately 5%.

Our clinical testing business, which accounted for over 90% of our 2007 net revenues, grew approximately 5.6% for the year, with AmeriPath contributing 8.3% growth and the change in status with UNH reducing revenues by approximately 5%. Volume, measured by the number of requisitions, declined 4.1% for the year ended December 31, 2007, primarily due to our change in status with UNH, which reduced volume by an estimated 7%, partially offset by the impact of the AmeriPath acquisition, which increased volume by about 3%. Revenue per requisition increased 10.2% for the year ended December 31, 2007 and was impacted by the results of AmeriPath, which contributed 5.1% to the improvement, and a 2% increase due to higher reimbursement on the retained business with UNH, which was reimbursed at a higher rate as a non-contracted provider, with the balance of the increase primarily driven by a positive test mix.

Our businesses other than clinical testing accounted for approximately 9% of net revenues in 2007. These businesses include our risk assessment services business, our clinical trials testing business, our healthcare information technology business, MedPlus, and our diagnostics products business. The revenues for these businesses as a group grew 23% for the year ended December 31, 2007 as compared to the prior year period, with the increase primarily driven by our acquisitions of HemoCue, Focus Diagnostics and Enterix.

Operating Costs and Expenses

Total operating costs and expenses for the year ended December 31, 2007 increased $473 million from the prior year period. Costs associated with the acquired operations of AmeriPath, Focus Diagnostics, Enterix and HemoCue increased costs by approximately $552 million for the year ended December 31, 2007. This increase was offset in part by actions taken to improve our operating efficiency and reduce the size of our workforce. Results for the year ended December 31, 2007 include first quarter charges of $10.7 million associated with workforce reductions ($3.9 million included in costs of services and $6.8 million in selling, general and administrative) and $4.0 million of in-process research and development costs associated with the acquisition of HemoCue, which was recorded in other operating (income) expense, net.

Cost of services, which includes the costs of obtaining, transporting and testing specimens, was 59.2% of net revenues for the year ended December 31, 2007, compared to 59.0% of net revenues in 2006. The increase in cost of services as a percentage of revenues was primarily due to lower volumes in our clinical testing business and costs

associated with workforce reductions. Partially offsetting these increases were improvements related to the increase in average revenue per requisition and actions taken to reduce costs.

Selling, general and administrative expenses, which include the costs of the sales force, billing operations, bad debt expense and general management and administrative support, were 24.1% of net revenues during the year ended December 31, 2007, compared to 22.5% in the prior year period. This increase was primarily due to lower volume levels in our clinical testing business; costs associated with workforce reductions; costs associated with efforts to retain business and clarify for patients, physicians and employers misinformation regarding the UNH contract change; and the impact of the acquired operations of AmeriPath and HemoCue.

For the year ended December 31, 2007, bad debt expense was 4.5% of net revenues, compared to 3.9% in the prior year period. The increase was principally driven by the inclusion of AmeriPath, which carries a higher bad debt rate than the rest of our business, primarily due to its revenue and customer mix, and by higher bad debt expense associated with billing patients directly for a portion of the UNH volume.

Other operating (income) expense, net represents miscellaneous income and expense items related to operating activities, including gains and losses associated with the disposal of operating assets and provisions for restructurings and other special charges. For the year ended December 31, 2007, other operating (income) expense, net included a $4.0 million charge related to in-process research and development expense recorded in connection with the acquisition of HemoCue. For the year ended December 31, 2006, other operating (income) expense, net included pre-tax charges of $27 million, principally associated with integration activities related to LabOne and our operations in California.

Operating Income

Operating income for the year ended December 31, 2007 was $1.1 billion, or 16.3% of net revenues, compared to $1.1 billion, or 18.0% of net revenues, in the prior year period. The decrease in operating income as a percentage of net revenues was principally due to lower volume levels in our clinical testing business, the various items which served to increase cost of services and selling, general and administrative expenses as a percentage of revenues, and the impact of the acquired operations of AmeriPath and HemoCue. These decreases were offset in part by actions we have taken to reduce our cost structure and higher revenue per requisition.

Other Income (Expense)

Interest expense, net for the year ended December 31, 2007 increased $87 million over the prior year. The increase in interest expense, net was primarily due to additional interest expense associated with borrowings to fund acquisitions, as described more fully in Note 9 to the Consolidated Financial Statements.

Other expense, net represents miscellaneous income and expense items related to non-operating activities such as gains and losses associated with investments and other non-operating assets. For the year ended December 31, 2007, other expense, net includes a $4 million charge related to the write-down of an investment. For the year ended December 31, 2006, other expense, net includes $26 million of charges related to the write-downs of investments partially offset by a gain of $16 million on the sale of an investment.

Discontinued Operations

In connection with the investigation of NID, which is described earlier, during the third quarter of 2007, the government and the Company began settlement discussions. In the course of those discussions, the government disclosed to the Company certain of the government s legal theories regarding the amount of damages allegedly incurred by the government, which include alleged violations of civil and criminal statutes including the False Claims Act and the Food, Drug and Cosmetics Act. Violations of these statutes and related regulations could lead to a warning letter, injunction, fines or penalties, exclusion from federal healthcare programs and/or criminal prosecution, as well as claims by third parties. The Company analyzed the government s position and presented its own analysis which argued against many of the government s claims. In light of that analysis and based on the status of settlement discussions, the Company established a reserve, in accordance with generally accepted accounting principles, reflected in discontinued operations, of $241 million in connection with these claims. See Note 14 and Note 15 to the Consolidated Financial Statements for a further description of these matters.

Loss from discontinued operations, net of tax, for the year ended December 31, 2007 was $214 million, or $1.10 per diluted share, compared to $39 million, or $0.20 per diluted share in 2006. Results for the year ended December 31, 2007 reflect a charge of $241 million to establish a reserve as described above. Results for the year ended December 31, 2006 reflect pre-tax charges of $32 million, primarily related to the wind down of NID s operations.

Quantitative and Qualitative Disclosures About Market Risk

We address our exposure to market risks, principally the market risk of changes in interest rates, through a controlled program of risk management that may include the use of derivative financial instruments. We do not hold or issue derivative financial instruments for trading purposes. We believe that our exposures to foreign exchange impacts and changes in commodities prices are not material to our consolidated financial condition or results of operations. See Note 10 to the Consolidated Financial Statements for additional discussion of our financial instruments and hedging activities.

At December 31, 2008 and 2007, the fair value of our debt was estimated at approximately $2.9 billion and $3.6 billion, respectively, using quoted market prices and yields for the same or similar types of borrowings, taking into account the underlying terms of the debt instruments. At December 31, 2008, the carrying value exceeded the estimated fair value of the debt by $155 million and at December 31, 2007, the estimated fair value exceeded the carrying value of the debt by $59 million. A hypothetical 10% increase in interest rates on our total debt portfolio (representing approximately 53 and 61 basis points at December 31, 2008 and 2007, respectively) would potentially reduce the estimated fair value of our debt by approximately $75 million and $78 million at December 31, 2008 and 2007, respectively.

Borrowings under our senior unsecured revolving credit facility, our secured receivables credit facility and our term loan due May 2012 are subject to variable interest rates. Interest on our secured receivables credit facility is based on rates that are intended to approximate commercial paper rates for highly-rated issuers. Interest rates on our senior unsecured revolving credit facility and term loan due May 2012 are subject to a pricing schedule that can fluctuate based on changes in our credit ratings. As such, our borrowing cost under these credit arrangements will be subject to both fluctuations in interest rates and changes in our credit ratings. As of December 31, 2008, the borrowing rates under these credit facilities were: for our secured receivables credit facility 3.6%; for our senior unsecured credit facility, LIBOR plus 0.40%; and for our term loan due May 2012, LIBOR plus 0.50%. At December 31, 2008, the weighted average LIBOR rate was 2.2%. At December 31, 2008, there was $1.1 billion outstanding under our term loan due May 2012, and no borrowings outstanding under our $500 million secured receivables credit facility and our $750 million senior unsecured revolving credit facility.

We have entered into various variable-to-fixed interest rate swap agreements, whereby we fixed the interest rates on $500 million of our term loan due May 2012 for periods through October 2009. As of December 31, 2008, variable-to-fixed interest rate swap agreements on $200 million of the term loan due May 2012 remain in place through October 2009 with fixed interest rates ranging from 5.13% to 5.27%. Based on our net exposure to interest rate changes, a hypothetical 10% change in interest rates on our variable rate indebtedness (representing approximately 25 basis points) would impact annual net interest expense by approximately $2.8 million, assuming no changes to the debt outstanding at December 31, 2008.

The fair value of the interest rate swap agreements at December 31, 2008 was a liability of $5.9 million. A hypothetical 10% decrease in interest rates (representing approximately 18 basis points) would potentially increase the fair value of the liability of these instruments by approximately $0.4 million at December 31, 2008. A hypothetical 10% increase in interest rates would potentially decrease the fair value of the liability of these instruments by approximately $0.4 million at December 31, 2008. For details regarding our outstanding debt and our financial instruments, see Notes 9 and 10 to the Consolidated Financial Statements.

Risk Associated with Investment Portfolio

Our investment portfolio includes equity investments in publicly held companies that are classified as available-for-sale securities and other strategic equity holdings in privately held companies. These securities are exposed to price fluctuations and are generally concentrated in the life sciences industry. The carrying values of our available-for-sale equity securities and privately held securities were $16 million at December 31, 2008.

We regularly evaluate the fair value measurements of our equity investments to determine if losses in value are other than temporary and if an impairment loss has been incurred. The evaluation considers if the security has the ability to recover and, if so, the estimated recovery period. Other factors that are considered in this evaluation include the amount of the other-than-temporary decline and its duration, the issuer s financial condition and short-term prospects and whether the market decline was caused by overall economic conditions or conditions specific to the individual security.

We do not hedge our equity price risk. The impact of an adverse movement in equity prices on our holdings in privately held companies cannot be easily quantified, as our ability to realize returns on investments depends on, among other things, the enterprises ability to raise additional capital or derive cash inflows from continuing operations or through liquidity events such as initial public offerings, mergers or private sales.

Fair Value Measurements

On January 1, 2008, we adopted SFAS No. 157, Fair Value Measurements. Adoption of this accounting standard did not have a material effect on our financial position, results of operations or cash flows. See Note 2 to the Consolidated Financial Statements for further details.

SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159) became effective for the Company on January 1, 2008. As of January 1, 2008 and for the year ended December 31, 2008, the Company has elected not to apply the fair value option to any of its financial assets or financial liabilities on-hand, which were not already measured at fair value, because the Company does not believe that application of SFAS 159 s fair value option is appropriate given the nature of its business operations. See Note 2 to the Consolidated Financial Statements for further details.

Liquidity and Capital Resources

Cash and Cash Equivalents

Cash and cash equivalents at December 31, 2008 totaled $254 million, compared to $168 million at December 31, 2007. Cash and cash equivalents consist of highly liquid short-term investments, including time deposits with highly-rated banks, and various insured money market funds, including those that invest in U.S. Treasury securities. The Company has not suffered any losses associated with its cash and cash equivalents. Cash flows from operating activities in 2008 were $1.1 billion, which were used to fund investing and financing activities of $199 million and $778 million, respectively. Cash and cash equivalents at December 31, 2007 totaled $168 million, compared to $150 million at December 31, 2006. Cash flows from operating activities in 2007 were $927 million which, together with $850 million of cash flows from financing activities, were used to fund investing activities of $1.8 billion.

Cash Flows from Operating Activities

Net cash provided by operating activities for 2008 was $1.1 billion compared to $927 million in 2007. This increase was primarily due to higher earnings in the current year. Net cash provided by operating activities for the year ended December 31, 2007 was reduced by $57 million of fees and other expenses paid in connection with the acquisition of AmeriPath. Days sales outstanding, a measure of billing and collection efficiency, were 44 days at December 31, 2008 compared to 48 days at December 31, 2007.

Net cash provided by operating activities for 2007 was $927 million compared to $952 million in 2006. This decrease was primarily due to lower earnings in 2007 and increased payments associated with variable compensation earned in the prior year, coupled with the payment of $57 million of fees and other expenses associated with the acquisition of AmeriPath. Partially offsetting these items was a net source of funds from reductions in net accounts receivable in the current year compared to a net use of funds in the prior year.

Cash Flows from Investing Activities

Net cash used in investing activities in 2008 was $199 million, consisting principally of capital expenditures of $213 million, partially offset by $23 million related to the receipt of a payment from an escrow fund established at the time of the acquisition of HemoCue.

Net cash used in investing activities in 2007 was $1.8 billion, consisting primarily of $1.2 billion related to the acquisition of AmeriPath, $309 million related to the acquisition of HemoCue and capital expenditures of $219 million.

Cash Flows from Financing Activities

Net cash used in financing activities in 2008 was $778 million, consisting primarily of net reductions of debt of $459 million. Debt repayments of $482 million, consisting primarily of the repayment of $120 million on our Secured Receivables Credit Facility, $60 million on our term loan due December 31, 2008 and $293 million on our term loan due May 31, 2012, were partially offset by borrowings of $20 million under our Secured Receivables Credit Facility. Since the completion of the AmeriPath acquisition in May 2007, we have reduced our total debt by $876 million.

Net cash used by financing activities for the year ended December 31, 2008 also included $33 million in proceeds from the exercise of stock options, including related tax benefits, offset by purchases of treasury stock totaling $254 million and dividend payments of $78 million. The $254 million of treasury stock purchases represents 5.5 million shares of our common stock purchased at an average price of $46.09 per share.

Net cash provided by financing activities in 2007 was $850 million, primarily associated with new borrowings and repayments related to the acquisitions of AmeriPath and HemoCue.

During the first quarter of 2007, we entered into an interim credit facility (the Interim Credit Facility) and borrowed $450 million to finance the acquisition of HemoCue and to repay substantially all of HemoCue s outstanding debt.

During the second quarter of 2007, we borrowed $1.6 billion under a five-year term loan facility and $780 million under a bridge loan facility to finance the acquisition of AmeriPath and repay the Interim Credit Facility used to finance the HemoCue acquisition.

In connection with the acquisition of AmeriPath, we repaid substantially all of AmeriPath s outstanding debt and related accrued interest. On May 21, 2007, we commenced a cash tender offer and consent solicitation for the $350 million aggregate principal amount of 10.5% Senior Subordinated Notes of AmeriPath, Inc. due 2013 (the AmeriPath senior subordinated notes). In conjunction with the cash tender offer, approximately $348 million in aggregate principal amount, or 99.4% of the $350 million outstanding under the AmeriPath senior subordinated notes, was tendered. We made payments of $386 million to holders with respect to the cash tender offer and consent solicitation, including tender premium and related solicitation fees and accrued interest.

We completed an $800 million senior notes offering in June 2007 (the 2007 Senior Notes). The 2007 Senior Notes were sold in two tranches: (a) $375 million of 6.40% senior notes due 2017; and (b) $425 million of 6.95% senior notes due 2037. We used the net proceeds from the 2007 Senior Notes offering to repay the $780 million of borrowings under the bridge loan facility. The 2007 Senior Notes, term loans and the bridge loan are further described in Note 9 to the Consolidated Financial Statements.

Net cash provided by financing activities for the year ended December 31, 2007 also included $95 million in proceeds from the exercise of stock options, including related tax benefits, offset by purchases of treasury stock totaling $146 million and dividend payments of $77 million. The $146 million of treasury stock purchases represents 2.8 million shares of our common stock purchased at an average price of $52.14 per share.

Dividend Program

During each of the quarters of 2008 and 2007, our Board of Directors declared a quarterly cash dividend of $0.10 per common share. We expect to fund future dividend payments with cash flows from operations, and do not expect the dividend to have a material impact on our ability to finance future growth.

Share Repurchase Plan

For the year ended December 31, 2008, we repurchased 5.5 million shares of our common stock at an average price of $46.09 per share for $254 million. Through December 31, 2008, we have repurchased 49.6 million shares of our common stock at an average price of $45.43 for $2 billion under our share repurchase program. During the fourth quarter of 2008, our Board of Directors expanded our share repurchase authorization by an additional $150 million, which together with the amounts remaining from previous authorizations, was fully utilized prior to December 31, 2008. In January 2009, our Board of Directors authorized $500 million of additional share repurchases.

Contractual Obligations and Commitments

The following table summarizes certain of our contractual obligations as of December 31, 2008. See Notes 9 and 14 to the Consolidated Financial Statements for further details.

	Payments due by period				
	(in thousands)				
Contractual Obligations	**Total**	**Less than 1 year**	**1 3 years**	**3 5 years**	**After 5 years**
Long-term debt	$ 3,065,070	$ 1,800	$ 1,206,449	$ 560,000	$ 1,296,821
Capital lease obligations	18,161	3,342	3,173	2,067	9,579
Interest payments on outstanding debt	1,446,716	159,887	280,256	169,488	837,085
Operating leases	634,579	174,025	245,683	108,745	106,126
Purchase obligations	82,088	42,849	32,831	5,939	469
Total contractual obligations	$ 5,246,614	$ 381,903	$ 1,768,392	$ 846,239	$ 2,250,080

Interest payments on our long-term debt have been calculated after giving effect to our interest rate swap agreements, using the interest rates as of December 31, 2008 applied to the December 31, 2008 balances, which are assumed to remain outstanding through their maturity dates.

As of December 31, 2008, our total liabilities for unrecognized tax benefits were approximately $71 million, which were excluded from the table above. Based upon the expiration of statutes of limitations, settlements and/or the conclusion of tax examinations, we believe it is reasonably possible that this amount may decrease by up to $34 million within the next twelve months. For the remainder, we cannot make reasonably reliable estimates of the timing of the

future payments of these liabilities. See Note 4 to the Consolidated Financial Statements for information regarding our contingent tax liability reserves.

As of December 31, 2008, the reserve for the settlement and related matters in connection with the investigation of NID of $316 million has been excluded from the table above. See Note 14 to the Consolidated Financial Statements for additional information.

Our credit agreements relating to our senior unsecured revolving credit facility and our term loan due May 2012 contain various covenants and conditions, including the maintenance of certain financial ratios, that could impact our ability to, among other things, incur additional indebtedness. We do not expect these covenants to adversely impact our ability to execute our growth strategy or conduct normal business operations.

Unconsolidated Joint Ventures

We have investments in unconsolidated joint ventures in Phoenix, Arizona; Indianapolis, Indiana; and Dayton, Ohio, which are accounted for under the equity method of accounting. We believe that our transactions with our joint ventures are conducted at arm s length, reflecting current market conditions and pricing. Total net revenues of our unconsolidated joint ventures equal less than 6% of our consolidated net revenues. Total assets associated with our unconsolidated joint ventures are less than 2% of our consolidated total assets. We have no material unconditional obligations or guarantees to, or in support of, our unconsolidated joint ventures and their operations.

Requirements and Capital Resources

We estimate that we will invest approximately $200 million during 2009 for capital expenditures to support and expand our existing operations, principally related to investments in information technology, equipment, and facility upgrades. During 2008, we continued to make investments in support of our plans to develop and deploy standard systems across both the AmeriPath practices and our clinical laboratories. We have completed the enhancements to the AmeriPath laboratory and billing systems and began deployment of the enhanced systems during the second quarter of 2008. These investments will enable significant productivity gains and improved customer service.

In June 2008, we amended our existing receivables securitization facility and increased it from $375 million to $400 million. The secured receivables credit facility was supported by back-up facilities provided on a committed basis by two banks: (a) $125 million, which matured on December 13, 2008 and (b) $275 million, which originally matured on June 10, 2009.

In December 2008, we replaced the $125 million portion of our secured receivables credit facility and amended the existing receivables securitization facility to increase it from $400 million to $500 million. The secured receivables credit facility continues to be supported by back-up facilities provided on a committed basis by two banks: (a) $225 million, which matures on December 11, 2009 and (b) $275 million, which also matures on December 11, 2009. Interest on the secured receivables credit facility is based on rates that are intended to approximate commercial paper rates for highly-rated issuers.

As of December 31, 2008, $1.3 billion of borrowing capacity was available under our existing credit facilities, consisting of $500 million available under our secured receivables credit facility and $750 million available under our senior unsecured revolving credit facility. No borrowings are currently outstanding under either facility.

We believe the banks participating in our various credit facilities are predominantly highly-rated banks, and that the entire amounts under the credit facilities are currently available to us. Should one or several banks no longer participate in either of our credit facilities, we would not expect it to impact our ability to fund operations. We expect to continue to generate positive cash flow despite a slowing economy, and have only $5 million of debt maturing over the next twelve months. We expect to be able to fund payments associated with the agreement in principle related to NID, out of cash on-hand and available credit facilities.

We believe that cash and cash equivalents on-hand and cash from operations, together with our borrowing capacity under our credit facilities, will provide sufficient financial flexibility to meet seasonal working capital requirements and to fund capital expenditures, debt service requirements, cash dividends on common shares, share repurchases and additional growth opportunities for the foreseeable future. We believe that our credit profile should provide us with access to additional financing, if necessary, to fund growth opportunities that cannot be funded from existing sources.

Outlook

As discussed in the Overview, despite the continued consolidation among healthcare insurers, and their continued efforts to reduce reimbursement for providers of diagnostic testing, and the general economic conditions, we believe that the underlying fundamentals of the diagnostic testing industry will continue to improve and that over the long

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term the industry will continue to grow. As the world s leading provider of diagnostic testing, information and services, we believe we are well positioned to benefit from the growth expected in our industry.

We believe our focus on delivering a superior patient experience and Six Sigma quality as well as the investments we are continuing to make in our distribution network, our industry leading test menu and our information technology solutions will further differentiate us over the long-term and strengthen our industry leadership position. In addition, we plan to leverage our knowledge and expertise in diagnostic testing to further expand into international markets and point-of-care testing.

Our strong cash generation, balance sheet and credit profile position us well to take advantage of these growth opportunities.

Inflation

We believe that inflation generally does not have a material adverse effect on our results of operations or financial condition because the majority of our contracts are short term.

Impact of New Accounting Standards

In September 2007, the Financial Accounting Standards Board (FASB) ratified Emerging Issues Task Force (EITF) Issue No. 07-1 Accounting for Collaborative Agreements. In December 2007, the FASB issued SFAS No. 141(R) Business Combinations and SFAS No. 160 Noncontrolling interests in Consolidated Financial Statements, an Amendment of ARB No. 51. In February 2008, the FASB issued FASB Staff Position (FSP) No. FAS 157-2 Effective Date of FASB Statement No. 157. In March 2008, the FASB issued SFAS No. 161, Disclosures About Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133. In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles. In June 2008, the FASB issued FSP EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities. In October 2008, the FASB issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. In November 2008, the FASB ratified the consensus reached under EITF Issue No. 08-7, Accounting for Defensive Intangible Assets. In December 2008, the FASB issued FSP No. FAS 140-4 and FIN 46(R)-8, Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities. The impact of these accounting standards is discussed in Note 2 to the Consolidated Financial Statements.

REPORT OF MANAGEMENT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Quest Diagnostics Incorporated (the Company), including its Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. Management assessed the effectiveness of the Company s internal control over financial reporting as of December 31, 2008 based on criteria for effective internal control over financial reporting described in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management has determined that the Company s internal control over financial reporting as of December 31, 2008 is effective.

The Company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America and that receipts and expenditures of the Company are being made only in accordance with authorization of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP, the independent registered public accounting firm that audited the financial statements included in this annual report, audited the Company s internal control over financial reporting as of December 31, 2008 and issued their audit report expressing an unqualified opinion on the Company s internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
Of Quest Diagnostics Incorporated

In our opinion, the consolidated financial statements listed in the index appearing under Item 15(a) (1) present fairly, in all material respects, the financial position of Quest Diagnostics Incorporated and its subsidiaries at December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2008 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for these financial statements and the financial statement schedule, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express opinions on these financial statements, on the financial statement schedule, and on the Company s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 2 to the consolidated financial statements, the Company changed the manner in which it accounts for uncertain tax positions in 2007.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Florham Park, New Jersey
February 17, 2009

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2008 AND 2007
(in thousands, except per share data)

	2008	2007
Assets		
Current assets:		
Cash and cash equivalents	$ 253,946	$ 167,594
Accounts receivable, net of allowance for doubtful accounts of $261,334 and $250,067 at December 31, 2008 and 2007, respectively	832,873	881,967
Inventories	102,125	95,234
Deferred income taxes	218,419	149,841
Prepaid expenses and other current assets	89,456	79,721
Total current assets	1,496,819	1,374,357
Property, plant and equipment, net	879,687	911,998
Goodwill, net	5,054,926	5,220,104
Intangible assets, net	827,403	886,733
Other assets	144,995	172,501
Total assets	$ 8,403,830	$ 8,565,693
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 1,219,619	$ 1,124,716
Short-term borrowings and current portion of long-term debt	5,142	163,581
Total current liabilities	1,224,761	1,288,297
Long-term debt	3,078,089	3,377,212
Other liabilities	496,084	575,942
Commitments and contingencies		
Stockholders equity:		
Common stock, par value $0.01 per share; 600,000 shares authorized at both December 31, 2008 and 2007; 214,113 shares and 213,745 shares issued at December 31, 2008 and 2007, respectively	2,141	2,137
Additional paid-in capital	2,262,065	2,210,825
Retained earnings	2,561,679	2,057,744
Accumulated other comprehensive (loss) income	(68,068)	25,279
Treasury stock, at cost; 23,739 shares and 19,705 shares at December 31, 2008 and 2007, respectively	(1,152,921)	(971,743)
Total stockholders equity	3,604,896	3,324,242
Total liabilities and stockholders equity	$ 8,403,830	$ 8,565,693

The accompanying notes are an integral part of these statements.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006
(in thousands, except per share data)

	2008	2007	2006
Net revenues	$ 7,249,447	$ 6,704,907	$ 6,268,659
Operating costs and expenses:			
Cost of services	4,256,156	3,969,848	3,696,006
Selling, general and administrative	1,736,934	1,612,858	1,410,716
Amortization of intangible assets	37,293	27,904	10,843
Other operating (income) expense, net	(3,312)	2,961	23,017
Total operating costs and expenses	6,027,071	5,613,571	5,140,582
Operating income	1,222,376	1,091,336	1,128,077
Other income (expense):			
Interest expense, net	(179,764)	(178,314)	(91,425)
Minority share of income	(31,705)	(26,510)	(23,900)
Equity earnings in unconsolidated joint ventures	29,736	26,969	28,469
Other expense, net	(21,691)	(1,079)	(7,948)
Total non-operating expenses, net	(203,424)	(178,934)	(94,804)
Income from continuing operations before taxes	1,018,952	912,402	1,033,273
Income tax expense	386,768	358,574	407,581
Income from continuing operations	632,184	553,828	625,692
Loss from discontinued operations, net of taxes	(50,694)	(213,889)	(39,271)
Net income	$ 581,490	$ 339,939	$ 586,421
Earnings per common share - basic:			
Income from continuing operations	$ 3.25	$ 2.87	$ 3.18
Loss from discontinued operations	(0.26)	(1.11)	(0.20)
Net income	$ 2.99	$ 1.76	$ 2.98
Earnings per common share - diluted:			
Income from continuing operations	$ 3.23	$ 2.84	$ 3.14
Loss from discontinued operations	(0.26)	(1.10)	(0.20)
Net income	$ 2.97	$ 1.74	$ 2.94
Dividends per common share	$ 0.40	$ 0.40	$ 0.40

The accompanying notes are an integral part of these statements.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006
(in thousands)

	2008	2007	2006
Cash flows from operating activities:			
Net income	$ 581,490	$ 339,939	$ 586,421
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	264,593	237,879	197,398
Provision for doubtful accounts	326,228	300,226	243,443
Provision for restructuring and other special charges	72,650	238,781	55,788
Deferred income tax provision (benefit)	549	(1,575)	(46,280)
Minority share of income	31,705	26,510	23,900
Stock compensation expense	70,581	56,853	55,478
Excess tax benefits from stock-based compensation arrangements	(2,420)	(13,981)	(32,693)
Other, net	13,772	8,310	20,172
Changes in operating assets and liabilities:			
Accounts receivable	(282,634)	(265,347)	(273,232)
Accounts payable and accrued expenses	(4,342)	(5,431)	81,347
Integration, settlement and other special charges	(8,223)	(14,013)	(4,247)
Income taxes payable	24,653	3,213	45,330
Other assets and liabilities, net	(25,553)	15,560	(929)
Net cash provided by operating activities	1,063,049	926,924	951,896
Cash flows from investing activities:			
Business acquisitions, net of cash acquired	8,066	(1,535,826)	(236,543)
Capital expenditures	(212,681)	(219,101)	(193,422)
Decrease (increase) in investments and other assets	5,732	(4,266)	15,563
Net cash used in investing activities	(198,883)	(1,759,193)	(414,402)
Cash flows from financing activities:			
Proceeds from borrowings	22,929	3,754,490	375,000
Repayments of debt	(481,870)	(2,705,369)	(416,208)
Increase (decrease) in book overdrafts	14,201	(24,950)	(1,705)
Purchases of treasury stock	(253,997)	(145,660)	(472,325)
Exercise of stock options	30,511	80,928	102,324
Excess tax benefits from stock-based compensation arrangements	2,420	13,981	32,693
Dividends paid	(77,964)	(77,327)	(77,135)
Distributions to minority partners	(32,931)	(24,678)	(21,900)
Financing costs paid	(1,113)	(21,192)	(728)
Net cash (used in) provided by financing activities	(777,814)	850,223	(479,984)
Net change in cash and cash equivalents	86,352	17,954	57,510
Cash and cash equivalents, beginning of year	167,594	149,640	92,130
Cash and cash equivalents, end of year	$ 253,946	$ 167,594	$ 149,640

The accompanying notes are an integral part of these statements.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006
(in thousands)

	Shares of Common Stock Outstanding	Common Stock	Additional Paid-In Capital	Retained Earnings	Unearned Compen-sation	Accumulated Other Compre-hensive (Loss) Income	Treasury Stock	Compre-hensive Income
Balance, December 31, 2005	198,455	$ 2,137	$ 2,175,533	$ 1,292,510	$ (3,321)	$ (6,205)	$ (697,670)	
Net income				586,421				$ 586,421
Currency translation						2,460		2,460
Market valuation, net of tax benefit of $2,501						(3,815)		(3,815)
Reversal of market adjustment, net of tax expense of $(5,053)						7,707		7,707
Deferred gain reclassifications						(212)		(212)
Comprehensive income								$ 592,561
Dividends declared				(78,676)				
Reclassification upon adoption of SFAS123R			(3,321)		3,321			
Issuance of common stock under benefit plans	598	1	(2,158)				23,838	
Stock-based compensation expense			55,478					
Exercise of stock options	3,782		(75,603)				177,927	
Shares to cover employee payroll tax withholdings on stock issued under benefit plans	(13)		(672)					
Tax benefits associated with stock-based compensation plans			35,816					
Purchases of treasury stock	(8,873)						(472,325)	
Balance, December 31, 2006	193,949	2,138	2,185,073	1,800,255		(65)	(968,230)	
Net income				339,939				$ 339,939
Currency translation						30,820		30,820
Market valuation, net of tax benefit of $24						(36)		(36)
Reversal of market adjustment, net of tax expense of $(510)						802		802
Deferred loss, less reclassifications						(6,242)		(6,242)
Comprehensive income								$ 365,283
Dividends declared				(77,304)				
Issuance of common stock under benefit plans	462		(1,974)				21,989	
Stock-based compensation expense			56,853					
Exercise of stock options	2,447		(39,230)				120,158	
Shares to cover employee payroll tax withholdings on stock issued under benefit plans	(24)	(1)	(1,229)					
Tax benefits associated with stock-based compensation plans			16,703					
Purchases of treasury stock	(2,794)						(145,660)	
Adjustments upon adoption of FASB Interpretation No. 48			(10,441)	(5,146)				
Reimbursement from Corning Incorporated			2,345					
Other			2,725					

Balance, December 31, 2007	194,040	2,137	2,210,825	2,057,744		25,279	(971,743)	
Net income				581,490				$ 581,490
Currency translation						(94,326)		(94,326)
Market valuation, net of tax benefit of $261						(398)		(398)
Reversal of market adjustment, net of tax expense of $(1,257)						2,161		2,161
Deferred loss, less reclassifications						(784)		(784)
Comprehensive income								$ 488,143
Dividends declared				(77,555)				
Issuance of common stock under benefit plans	913	4	81				18,248	
Stock-based compensation expense			63,055				7,526	
Exercise of stock options	987		(18,148)				48,659	
Shares to cover employee payroll tax withholdings on stock issued under benefit plans	(56)		(962)				(1,614)	
Tax benefits associated with stock-based compensation plans			6,881					
Purchases of treasury stock	(5,510)						(253,997)	
Other			333					
Balance, December 31, 2008	190,374	$ 2,141	$ 2,262,065	$ 2,561,679	$	$ (68,068)	$ (1,152,921)	

The accompanying notes are an integral part of these statements.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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(dollars in thousands unless otherwise indicated)

1. DESCRIPTION OF BUSINESS

Quest Diagnostics Incorporated and its subsidiaries (Quest Diagnostics or the Company) is the world s leading provider of diagnostic testing, information and services, providing insights that enable patients, physicians and others to make decisions to improve health. Quest Diagnostics offers patients and physicians the broadest access to diagnostic laboratory services through the Company s nationwide network of laboratories and owned patient service centers. The Company provides interpretive consultation through the largest medical and scientific staff in the industry, with approximately 900 M.D.s and Ph.D.s primarily located in the United States. Quest Diagnostics is the leading provider of clinical testing, including gene-based testing and other esoteric testing, anatomic pathology services and testing for drugs-of-abuse, and the leading provider of risk assessment services for the life insurance industry. The Company is also a leading provider of testing for clinical trials. The Company s diagnostics products business manufactures and markets diagnostic test kits and specialized point-of-care testing. Quest Diagnostics empowers healthcare organizations and clinicians with state-of-the-art information technology solutions that can improve patient care and medical practice.

During 2008, Quest Diagnostics processed approximately 150 million requisitions through its extensive network of laboratories in virtually every major metropolitan area throughout the United States.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of all entities controlled by the Company through its direct or indirect ownership of a majority voting interest and the accounts of any variable interest entities, as defined in Financial Accounting Standards Board (FASB) Interpretation No. 46 Consolidation of Variable Interest Entities, where the Company is subject to a majority of the risk of loss from the variable interest entity s activities, or entitled to receive a majority of the entity s residual returns or both. The Company s relationships with variable interest entities were not material at both December 31, 2008 and 2007. Investments in entities which the Company does not control, but in which it has a substantial ownership interest (generally between 20% and 49%) and can exercise significant influence, are accounted for using the equity method of accounting. As of December 31, 2008 and 2007, the Company s investments in affiliates accounted for under the equity method of accounting totaled $38.4 million and $37.5 million, respectively. The Company s share of equity earnings from investments in affiliates, accounted for under the equity method, totaled $29.7 million, $27.0 million and $28.5 million, respectively, for 2008, 2007 and 2006. All significant intercompany accounts and transactions are eliminated in consolidation.

Basis of Presentation

During the third quarter of 2006, the Company completed its wind-down of NID, a test kit manufacturing subsidiary, and classified the operations of NID as discontinued operations. The accompanying consolidated statements of operations and related disclosures have been prepared to report the results of NID as discontinued operations for all periods presented. See Note 15 for a further discussion of discontinued operations.

In addition, certain reclassifications have been made to conform to the current year presentation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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Revenue Recognition

The Company primarily recognizes revenue for services rendered upon completion of the testing process. Billings for services reimbursed by third-party payers, including Medicare and Medicaid, are recorded as revenues net of allowances for differences between amounts billed and the estimated receipts from such payers. Adjustments to the estimated receipts, based on final settlement with the third-party payers, are recorded upon settlement. In 2008, 2007 and 2006, approximately 18%, 17% and 17%, respectively, of the Company s net revenues were generated by Medicare and Medicaid programs. Under capitated arrangements with healthcare plans, the Company recognizes revenue based on a predetermined monthly reimbursement rate for each member of an insurer s health plan regardless of the number or cost of services provided by the Company.

Taxes on Income

The Company uses the asset and liability approach to account for income taxes. Under this method, deferred tax assets and liabilities are recognized for the expected future tax consequences of differences between the carrying amounts of assets and liabilities and their respective tax bases using tax rates in effect for the year in which the differences are expected to reverse. A valuation allowance is provided when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period when the change is enacted.

On January 1, 2007, the Company adopted FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 109 Accounting for Income Taxes. FIN 48 provides guidance on recognizing, measuring, presenting and disclosing in the financial statements uncertain tax positions that a company has taken or expects to take on a tax return. See Note 4 for further information related to FIN 48.

Earnings Per Share

Basic earnings per common share is calculated by dividing net income by the weighted average common shares outstanding. Diluted earnings per common share is calculated by dividing net income by the weighted average common shares outstanding after giving effect to all potentially dilutive common shares outstanding during the period. Potentially dilutive common shares include the dilutive effect of outstanding stock options, performance share units, restricted common shares and restricted stock units granted under the Company s Amended and Restated Employee Long-Term Incentive Plan and its Amended and Restated Director Long-Term Incentive Plan.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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The computation of basic and diluted earnings per common share was as follows (in thousands, except per share data):

	2008	2007	2006
Income from continuing operations	$ 632,184	$ 553,828	$ 625,692
Loss from discontinued operations	(50,694)	(213,889)	(39,271)
Net income available to common stockholders	$ 581,490	$ 339,939	$ 586,421
Weighted average common shares outstanding basic	194,283	193,241	196,985
Effect of dilutive securities:			
Stock options	1,675	2,019	2,535
Restricted common shares, restricted stock units and performance share units	1	2	22
Weighted average common shares outstanding diluted	195,959	195,262	199,542
Earnings per common share basic:			
Income from continuing operations	$ 3.25	$ 2.87	$ 3.18
Loss from discontinued operations	(0.26)	(1.11)	(0.20)
Net income	$ 2.99	$ 1.76	$ 2.98
Earnings per common share diluted:			
Income from continuing operations	$ 3.23	$ 2.84	$ 3.14
Loss from discontinued operations	(0.26)	(1.10)	(0.20)
Net income	$ 2.97	$ 1.74	$ 2.94

The following securities were not included in the diluted earnings per share calculation due to their antidilutive effect (in thousands):

	2008	2007	2006
Stock options	2,676	3,114	2,443
Restricted common shares, restricted stock units and performance share units	1,339	731	786

Stock-Based Compensation

SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123), as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure an amendment of FASB Statement No. 123 (SFAS 148) encouraged, but did not require, companies to record compensation cost for stock-based compensation plans at fair value. In addition, SFAS 148 provided alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation, and amended the disclosure requirements of SFAS 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

In December 2004, the FASB issued SFAS No. 123, revised 2004, Share-Based Payment (SFAS 123R). SFAS 123R requires that companies recognize compensation cost relating to share-based payment transactions based on the fair value of the equity or liability instruments issued. The Company adopted SFAS 123R effective January 1, 2006 using the modified prospective approach and therefore has not restated

results for prior periods. Under this

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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approach, awards that are granted, modified or settled after January 1, 2006 will be measured and accounted for in accordance with SFAS 123R. Unvested awards that were granted prior to January 1, 2006 will continue to be accounted for in accordance with SFAS 123, as amended by SFAS 148, except that compensation cost will be recognized in the Company s results of operations.

Pursuant to the provisions of SFAS 123R, the Company records stock-based compensation as a charge to earnings net of the estimated impact of forfeited awards. As such, the Company recognizes stock-based compensation cost only for those stock-based awards that are estimated to ultimately vest over their requisite service period, based on the vesting provisions of the individual grants. The cumulative effect on current and prior periods of a change in the estimated forfeiture rate is recognized as compensation cost in earnings in the period of the revision. The terms of the Company s performance share unit grants allow the recipients of such awards to earn a variable number of shares based on the achievement of the performance goals specified in the awards. For performance share unit awards granted prior to 2008, the actual amount of any stock award earned is based on the Company s earnings per share growth as measured in accordance with its Amended and Restated Employee Long-Term Incentive Plan (ELTIP) for the performance period compared to that of a peer group of companies. Beginning with performance share unit awards granted in 2008, the performance measure for these awards will be based on the cumulative annual growth rate of the Company s earnings per share from continuing operations over a three year period. Stock-based compensation expense associated with performance share units is recognized based on management s best estimates of the achievement of the performance goals specified in such awards and the resulting number of shares that will be earned. The cumulative effect on current and prior periods of a change in the estimated number of performance share units expected to be earned is recognized as compensation cost in earnings in the period of the revision. The Company recognizes stock-based compensation expense related to the Company s Amended Employee Stock Purchase Plan (ESPP) based on the 15% discount at purchase. See Note 12 for a further discussion of stock-based compensation.

Fair Value Measurements

On January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements (SFAS 157). SFAS 157 provides a single definition of fair value and a common framework for measuring fair value as well as new disclosure requirements for fair value measurements used in financial statements. Fair value measurements are based upon the exit price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants exclusive of any transaction costs, and are determined by either the principal market or the most advantageous market. The principal market is the market with the greatest level of activity and volume for the asset or liability. Absent a principal market to measure fair value, the Company would use the most advantageous market, which is the market that the Company would receive the highest selling price for the asset or pay the lowest price to settle the liability, after considering transaction costs. However, when using the most advantageous market, transaction costs are only considered to determine which market is the most advantageous and these costs are then excluded when applying a fair value measurement. The adoption of SFAS 157 did not have a material effect on the Company s financial position, results of operations or cash flows.

In February 2008, the FASB issued FASB Staff Position (FSP) FAS 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13 (FSP FAS 157-1). FSP FAS 157-1 amended SFAS 157 to exclude from its scope SFAS No. 13, Accounting for Leases, and its related interpretive accounting pronouncements that address leasing transactions. However, this exclusion does not apply to the Company s impairment of long-lived assets under a capital lease pursuant to SFAS No. 144, Accounting for Impairment or Disposal of Long-Lived Assets, the Company s cost to terminate an operating lease under SFAS No. 146, Accounting for Costs Associated with Exit and Disposal Activities, and the measurement of acquired leases in a business combination pursuant to SFAS No. 141 or 141(R), Business Combinations. Also in February 2008, the FASB issued FSP FAS 157-2, Effective Date of FASB Statement No. 157 (FSP FAS 157-2). FSP FAS 157-2 amended SFAS 157 to defer the effective date of SFAS 157 for one year for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis, at least annually. The impact of SFAS 157 on the Company s non-financial assets and non-financial liabilities measured at fair value on a nonrecurring basis is not expected to have a material effect on the Company s financial position, results of operations or cash flows.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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SFAS 157 creates a three-level hierarchy to prioritize the inputs used in the valuation techniques to derive fair values. The basis for fair value measurements for each level within the hierarchy is described below with Level 1 having the highest priority and Level 3 having the lowest.

Level 1: Quoted prices in active markets for identical assets or liabilities.

Level 2: Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets.

Level 3: Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following table provides a summary of the recognized assets and liabilities that are measured at fair value on a recurring basis.

		Basis of Fair Value Measurements		
		Quoted Prices in Active Markets for Identical Assets / Liabilities	Significant Other Observable Inputs	Significant Unobservable Inputs
	December 31, 2008	Level 1	Level 2	Level 3
Assets:				
Trading securities	$ 25,383	$ 25,383	$	$
Cash surrender value of life insurance policies	11,767		11,767	
Foreign currency forward contracts	2,617		2,617	
Available-for-sale securities	255	233	22	
Total	$ 40,022	$ 25,616	$ 14,406	$
Liabilities:				
Interest rate swaps	$ 5,888	$	$ 5,888	$
Foreign currency forward contracts	4,142		4,142	
Deferred compensation liabilities	39,304		39,304	
Total	$ 49,334	$	$ 49,334	$

The Company offers certain employees the opportunity to participate in a supplemental deferred compensation plan. A participant s deferrals, together with Company matching credits, are invested in a variety of participant-directed stock and bond mutual funds as well as Company common stock and are classified as trading securities. Changes in the fair value of these securities are measured using quoted prices in active markets based on the market price per unit multiplied by the number of units held exclusive of any transaction costs. A corresponding adjustment for changes in fair value of the trading securities is also reflected in the changes in fair value of the deferred compensation obligation. The deferred compensation liabilities are classified within Level 2 because their inputs are derived principally from observable market data by correlation to the trading securities.

In connection with the acquisition of AmeriPath Group Holdings, Inc. (AmeriPath) in May 2007, the Company assumed a non-qualified deferred compensation program AmeriPath offers to certain employees. A participant s deferrals, together with Company matching credits, are invested at the direction of the employee in a hypothetical portfolio of investments which are tracked by an administrator. The Company purchases life insurance policies, with the Company named as beneficiary of the policies, for the purpose of funding the program s liability.

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Changes in the cash surrender value of the life insurance policies are based upon earnings and changes in the value of the underlying investments. Changes in the fair value of the deferred compensation obligation are derived using quoted prices in active markets based on the market price per unit multiplied by the number of units. The cash surrender value and the deferred compensation obligations are classified within Level 2 because their inputs are derived principally from observable market data by correlation to the hypothetical investments.

The fair value measurements for available-for-sale securities are based upon the quoted price in active markets multiplied by the number of shares owned exclusive of any transaction costs and without any adjustments to reflect discounts that may be applied to selling a large block of the securities at one time. The Company does not believe that the changes in fair value of these assets will materially differ from the amounts that could be realized upon settlement or that the changes in fair value will have a material effect on the Company s results of operations, liquidity and capital resources.

The fair value measurements of foreign currency forward contracts are obtained from a third-party pricing service. The fair value measurements of the Company s interest rate swaps are model-derived valuations as of a given date in which all significant inputs are observable in active markets including certain financial information and certain assumptions regarding past, present and future market conditions. The Company does not believe that the changes in the fair values of its foreign currency forward contracts and interest rate swaps will materially differ from the amounts that could be realized upon settlement or maturity or that the changes in fair value will have a material effect on its results of operations, liquidity and capital resources.

SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159) became effective for the Company on January 1, 2008. SFAS 159 provides companies with an option to irrevocably elect to measure certain financial assets and financial liabilities at fair value on an instrument-by-instrument basis with the resulting changes in fair value recorded in earnings. The objective of SFAS 159 is to reduce both the complexity in accounting for financial instruments and the volatility in earnings caused by using different measurement attributes for financial assets and financial liabilities. As of January 1, 2008 and for the period ended December 31, 2008, the Company has elected not to apply the fair value option to any of its financial assets or financial liabilities on-hand, which were not already measured at fair value, because the Company does not believe that application of SFAS 159 s fair value option is appropriate, given the nature of its business operations.

The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable and accrued expenses approximate fair value based on the short maturities of these instruments. In accordance with the provisions of SFAS No. 107, Disclosures About Fair Value of Financial Instruments at December 31, 2008 and December 31, 2007, the fair value of the Company s debt was estimated at $2.9 billion and $3.6 billion, respectively, using quoted market prices and yields for the same or similar types of borrowings, taking into account the underlying terms of the debt instruments. At December 31, 2008, the carrying value exceeded the estimated fair value of the debt by $155 million and at December 31, 2007, the estimated fair value exceeded the carrying value of the debt by $59 million.

Foreign Currency

The Company predominately uses the U.S. dollar as its functional currency. The functional currency of the Company s foreign subsidiaries is the applicable local currency. Assets and liabilities denominated in non-U.S. dollars are translated into U.S. dollars at exchange rates as of the end of the reporting period. Income and expense items are translated at average exchange rates prevailing during the year. The translation adjustments are recorded as a component of accumulated other comprehensive (loss) income within stockholders equity. Gains and losses from foreign currency transactions are included within other operating (income) expense, net in the consolidated statements of operations. Transaction gains and losses have not been material.

Cash and Cash Equivalents

Cash and cash equivalents include all highly-liquid investments with original maturities, at the time acquired by the Company, of three months or less.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk are principally cash, cash equivalents, short-term investments and accounts receivable. The Company s policy is to place its cash, cash equivalents and short-term investments in highly-rated financial instruments and institutions. Concentration of credit risk with respect to accounts receivable is mitigated by the diversity of the Company s payers and their dispersion across many different geographic regions, and is limited to certain payers who are large buyers of the Company s services. To reduce risk, the Company routinely assesses the financial strength of these payers and, consequently, believes that its accounts receivable credit risk exposure, with respect to these payers, is limited. While the Company has receivables due from federal and state governmental agencies, the Company does not believe that such receivables represent a credit risk since the related healthcare programs are funded by federal and state governments, and payment is primarily dependent on submitting appropriate documentation.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are reported at realizable value, net of allowances for doubtful accounts, which is estimated and recorded in the period the related revenue is recorded. The Company has a standardized approach to estimate and review the collectibility of its receivables based on a number of factors, including the period they have been outstanding. Historical collection and payer reimbursement experience is an integral part of the estimation process related to allowances for doubtful accounts. In addition, the Company regularly assesses the state of its billing operations in order to identify issues which may impact the collectibility of these receivables or reserve estimates. Revisions to the allowances for doubtful accounts estimates are recorded as an adjustment to bad debt expense within selling, general and administrative expenses. Receivables deemed to be uncollectible are charged against the allowance for doubtful accounts at the time such receivables are written-off. Recoveries of receivables previously written-off are recorded as credits to the allowance for doubtful accounts.

Inventories

Inventories, which consist principally of testing supplies and reagents, are valued at the lower of cost (first in, first out method) or market.

Property, Plant and Equipment

Property, plant and equipment is recorded at cost. Major renewals and improvements are capitalized, while maintenance and repairs are expensed as incurred. Costs incurred for computer software developed or obtained for internal use are capitalized for application development activities and expensed as incurred for preliminary project activities and post-implementation activities. Capitalized costs include external direct costs of materials and services consumed in developing or obtaining internal-use software, payroll and payroll-related costs for employees who are directly associated with and who devote time to the internal-use software project, and interest costs incurred, when material, while developing internal-use software. Capitalization of such costs ceases when the project is substantially complete and ready for its intended purpose. Certain costs, such as maintenance and training, are expensed as incurred. The Company capitalizes interest on borrowings during the active construction period of major capital projects. Capitalized interest is added to the cost of the underlying assets and is amortized over the expected useful lives of the assets. Depreciation and amortization are provided on the straight-line method over expected useful asset lives as follows: buildings and improvements, ranging from ten to thirty years; laboratory equipment and furniture and fixtures, ranging from three to seven years; leasehold improvements, the lesser of the useful life of the improvement or the remaining life of the building or lease, as applicable; and computer software developed or obtained for internal use, ranging from three to seven years.

Goodwill

Goodwill represents the cost of acquired businesses in excess of the fair value of assets acquired, including separately recognized intangible assets, less the fair value of liabilities assumed in a business combination. The Company uses a nonamortization approach to account for purchased goodwill. Under a nonamortization approach, goodwill is not amortized, but instead is periodically reviewed for impairment.

QUEST DIAGNOSTICS INCORPORATED AND SUBSIDIARIES
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Intangible Assets

Intangible assets are recognized as an asset apart from goodwill if the asset arises from contractual or other legal rights, or if it is separable. Intangible assets, principally representing the cost of customer relationships, customer lists and non-competition agreements acquired, are capitalized and amortized on the straight-line method over their expected useful life, which generally ranges from five to twenty years. Intangible assets with indefinite useful lives, consisting principally of acquired tradenames, are not amortized, but instead are periodically reviewed for impairment.

Recoverability and Impairment of Goodwill

Under the nonamortization provisions of SFAS No. 142, Goodwill and Other Intangible Assets (SFAS 142), goodwill and certain intangibles are periodically reviewed for impairment and an impairment charge is recorded in the periods in which the recorded carrying value of goodwill and certain intangibles is more than its estimated fair value. The provisions of SFAS 142 require that a goodwill impairment test be performed annually or in the case of other events that indicate a potential impairment. The annual impairment tests of goodwill were performed at the end of each of the Company s fiscal years on December 31 and indicated that there was no impairment of goodwill as of December 31, 2008 or 2007.

The Company evaluates the recoverability and measures the potential impairment of its goodwill under SFAS 142. The annual impairment test is a two-step process that begins with the estimation of the fair value of the reporting unit. The first step screens for potential impairment and the second step measures the amount of the impairment, if any. Management s estimate of fair value considers publicly available information regarding the market capitalization of the Company as well as (i) the financial projections and future prospects of the Company s business, including its growth opportunities and likely operational improvements, and (ii) comparable sales prices, if available. As part of the first step to assess potential impairment, management compares the estimate of fair value for the reporting unit to the book value of the reporting unit. If the book value is greater than the estimate of fair value, the Company would then proceed to the second step to measure the impairment, if any. The second step compares the implied fair value of goodwill with its carrying value. The implied fair value is determined by allocating the fair value of the reporting unit to all of the assets and liabilities of that unit as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the purchase price paid to acquire the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. If the carrying amount of the reporting unit s goodwill is greater than its implied fair value, an impairment loss will be recognized in the amount of the excess. Management believes its estimation methods are reasonable and reflective of common valuation practices.

On a quarterly basis, management performs a review of the Company s business to determine if events or changes in circumstances have occurred which could have a material adverse effect on the fair value of the Company and its goodwill. If such events or changes in circumstances were deemed to have occurred, the Company would perform an impairment test of goodwill as of the end of the quarter, consistent with the annual impairment test, and record any noted impairment loss.

Recoverability and Impairment of Intangible Assets and Other Long-Lived Assets

The Company evaluates the possible impairment of its long-lived assets, including intangible assets which are amortized pursuant to the provisions of SFAS 142, under SFAS No. 144, Accounting for Impairment or Disposal of Long-Lived Assets. The Company reviews the recoverability of its long-lived assets when events or changes in circumstances occur that indicate that the carrying value of the asset may not be recoverable. Evaluation of possible impairment is based on the Company s ability to recover the asset from the expected future pretax cash flows (undiscounted and without interest charges) of the related operations. If the expected undiscounted pretax cash flows are less than the carrying amount of such asset, an impairment loss is recognized for the difference between the estimated fair value and carrying amount of the asset.

Investments

The Company accounts for investments in equity securities, which are included in other assets in the consolidated balance sheet, in conformity with SFAS No. 115, Accounting for Certain Investments in Debt and

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Equity Securities, which requires the use of fair value accounting for trading or available-for-sale securities. Both realized and unrealized gains and losses for trading securities are recorded currently in earnings as a component of non-operating expenses within other expense, net in the consolidated statements of operations. Unrealized gains and losses, net of tax, for available-for-sale securities are recorded as a component of accumulated other comprehensive (loss) income within stockholders equity. Recognized gains and losses for available-for-sale securities are recorded in other expense, net in the consolidated statements of operations. Gains and losses on securities sold are based on the average cost method.

The Company periodically reviews its investments to determine whether a decline in fair value below the cost basis is other than temporary. The primary factors considered in the determination are: the length of time that the fair value of the investment is below carrying value; the financial condition, operating performance and near term prospects of the investee; and the Company s intent and ability to hold the investment for a period of time sufficient to allow for a recovery in fair value. If the decline in fair value is deemed to be other than temporary, the cost basis of the security is written down to fair value.

Investments at December 31, 2008 and 2007 consisted of the following:

	2008	2007
Available-for-sale equity securities	$ 255	$ 9,690
Trading equity securities	25,383	33,903
Other investments	15,539	16,460
Total	$ 41,177	$ 60,053

Investments in available-for-sale equity securities consist of equity securities in public corporations. Investments in trading equity securities represent participant-directed investments of deferred employee compensation and related Company matching contributions held in a trust pursuant to the Company s supplemental deferred compensation plan (see Note 12). Other investments do not have readily determinable fair values and consist of investments in preferred and common shares of privately held companies and are accounted for under the cost method.

As of December 31, 2008 and 2007, the Company had gross unrealized losses from available-for-sale equity securities of $0.6 million and $3.5 million, respectively. For the year ended December 31, 2008 and 2007, other expense, net, within the consolidated statements of operations, includes $8.9 million and $4.0 million, respectively, of charges associated with the write-down of available-for-sale equity securities. For the year ended December 31, 2006, other expense, net, within the consolidated statements of operations, includes $16.2 million of charges associated with the write-down of available-for-sale equity securities, $10.0 million of charges associated with the write-down of other investments and a $15.8 million gain associated with the sale of an investment. For the years ended December 31, 2008, 2007 and 2006, (losses) gains from trading equity securities totaled $(9.9) million, $2.7 million and $3.2 million, respectively, and are included in other expense, net.

Derivative Financial Instruments

The Company uses derivative financial instruments to manage its market risks. This includes the use of interest rate swap agreements to manage its exposure to movements in interest rates and foreign currency forward contracts to manage its exposure to foreign exchange rates. The Company has established policies and procedures for risk assessment and the approval, reporting and monitoring of derivative financial instrument activities. These policies prohibit holding or issuing derivative financial instruments for speculative purposes.

Interest rate swaps involve the periodic exchange of payments without the exchange of underlying principal or notional amounts. Net payments are recognized as an adjustment to interest expense. When the swaps are terminated, unrealized gains or losses are deferred in stockholders equity, as a component of accumulated other comprehensive (loss) income, and are amortized as an adjustment to interest expense over the shorter of the remaining original term of the hedging instrument or the remaining life of the underlying debt instrument.

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The Company formally documents its hedge relationships, including identifying the hedging instruments and the hedged items, as well as its risk management objectives and strategies for undertaking the hedge transaction. On the date the derivative is entered into, the Company designates the type of derivative as a fair value hedge or cash flow hedge, and accounts for the derivative in accordance with its designation as prescribed by SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133), as amended. The Company currently holds only cash flow hedges, designated as a hedge of the variability of cash outflows related to the Company s long-term debt due to changes in interest rates. Both at inception and at least quarterly thereafter, the Company also formally assesses whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in the cash flows of the hedged item. All components of each derivative financial instrument s gain or loss are included in the assessment of hedge effectiveness.

The Company accounts for derivatives in conformity with SFAS No. 133, as amended, and records derivatives as either an asset or liability measured at its fair value. The fair value is based upon quoted market prices obtained from third-party institutions. For derivatives that have been formally designated as a cash flow hedge (interest rate swap agreements), the effective portion of changes in the fair value of the derivatives is recorded in accumulated other comprehensive (loss) income. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether a derivative is designated as part of a hedge transaction and, if it is, the type of hedge transaction based on the specific qualifying conditions in SFAS 133. Amounts in accumulated other comprehensive (loss) income are reclassified into earnings in interest expense, net during the same period in which the hedged item affects earnings. If it is determined that a derivative ceases to be a highly effective hedge, the Company discontinues hedge accounting, and any deferred gains or losses are recorded in the consolidated statement of operations.

Comprehensive Income (Loss)

Comprehensive income (loss) encompasses all changes in stockholders equity (except those arising from transactions with stockholders) and includes net income, net unrealized capital gains or losses on available-for-sale securities, foreign currency translation adjustments and deferred gains related to the settlement of certain treasury lock agreements (see Note 10).

New Accounting Standards

In September 2007, the FASB ratified Emerging Issues Task Force Issue No. 07-1 Accounting for Collaborative Agreements, (EITF 07-1). EITF 07-1 defines collaborative agreements as contractual arrangements that involve a joint operating activity. These arrangements involve two (or more) parties that are both active participants in the activity and are exposed to significant risks and rewards dependent on the commercial success of the activity. EITF 07-1 provides guidance that revenues generated and costs incurred by participants from transactions with parties outside the collaborative agreement should be reported either on a gross basis or a net basis depending on whether the participant is a principal or agent to the transaction. EITF 07-1 also provides that a company should report the effects of adoption as a change in accounting principle through retrospective application to all periods and requires additional disclosures about a company s collaborative arrangements. EITF 07-1 is effective for the Company as of January 1, 2009. The adoption of EITF 07-1 is not expected to have a material impact on the Company s consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141(R) Business Combinations (SFAS 141(R)). SFAS 141(R) changes several underlying principles in applying the purchase method of accounting. Among the significant changes, SFAS 141(R) requires a redefining of the measurement date of a business combination, expensing direct transaction costs as incurred, capitalizing in-process research and development costs as an intangible asset and recording a liability for contingent consideration at the measurement date with subsequent re-measurements recorded in the results of operations. SFAS 141(R) also requires that costs for business restructuring and exit activities related to the acquired company will be included in the post-combination financial results of operations and also provides new guidance for the recognition and measurement of contingent assets and liabilities in a business combination. In addition, adjustments to acquisition-related tax contingencies and deferred tax valuation allowances for both past and prospective business combinations will no longer be an adjustment to goodwill, but rather reflected in earnings in the period of adjustment. SFAS 141(R) requires several new disclosures, including the reasons for the business combination, the factors that contribute to the recognition of goodwill, the amount of acquisition related third-party

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expenses incurred, the nature and amount of contingent consideration, and a discussion of pre-existing relationships between the parties. SFAS 141(R) is effective for the Company as of January 1, 2009. The Company expects that the adoption of SFAS 141(R) is likely to have a significant impact on how the Company allocates the purchase price of an acquired business, including the expensing of direct transaction costs and costs to integrate the acquired business. Transaction costs for potential business combinations that had not closed by December 31, 2008 were written off on January 1, 2009 and were not material.

In December 2007, the FASB issued SFAS No. 160 Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51, (SFAS 160). SFAS 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 requires noncontrolling interests in subsidiaries initially to be measured at fair value and classified as a separate component of equity. SFAS 160 also requires a new presentation on the face of the consolidated financial statements to separately report the amounts attributable to controlling and non-controlling interests. SFAS 160 is effective for the Company as of January 1, 2009. The adoption of SFAS 160 is not expected to have a material impact on the Company s consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161 Disclosures About Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, by requiring expanded disclosures about an entity s derivative instruments and hedging activities. SFAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments. SFAS 161 is effective for the Company as of January 1, 2009. The adoption of SFAS 161 is not expected to have a material impact on the Company s consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162 The Hierarchy of Generally Accepted Accounting Principles (SFAS 162). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (the GAAP hierarchy). SFAS 162 will become effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board amendments to AICPA Professional Standards AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. The adoption of SFAS 162 is not expected to have a material impact on the Company s consolidated financial statements.

In June 2008, the FASB issued FSP EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (FSP EITF 03-6-1). FSP EITF 03-6-1 addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in computing earnings per share under the two-class method described in SFAS No. 128, Earnings Per Share. FSP EITF 03-6-1 is effective for the Company as of January 1, 2009 and in accordance with its requirements it will be applied retrospectively. The Company does not expect the adoption of FSP EITF 03-6-1 to have a material impact on its consolidated financial statements.

In October 2008, the FASB issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active (FSP FAS 157-3). FSP FAS 157-3 clarifies the application of SFAS 157 in a market that is not active and illustrates how an entity would determine fair value when the market for a financial asset is not active. FSP FAS 157-3 provides guidance on how an entity s own assumptions about cash flows and discount rates should be considered when measuring fair value when relevant market data does not exist, how observable market information in an inactive or dislocated market affects fair value measurements and how the use of broker and pricing service quotes should be considered when applying fair value measurements. FSP FAS 157-3 was effective immediately as of September 30, 2008 and for all interim and annual periods thereafter. The adoption of FSP FAS 157-3 did not have a material impact on the Company s consolidated financial statements.

In November 2008, the FASB ratified the consensus reached under EITF Issue No. 08-7, Accounting for Defensive Intangible Assets (EITF 08-7). EITF 08-7 requires that certain intangible assets acquired in a business

combination that will be held for defensive purposes shall be measured at their fair value when they are obtained. The useful life of a defensive intangible asset will be based on the period in which the asset is expected to directly or indirectly contribute to future cash flows up through the date it is effectively abandoned. EITF 08-7 is effective for the Company as of January 1, 2009. The purchase price allocations in prospective business combinations will require the Company to ascribe a fair value to intangible assets it intends to hold for defensive purposes and to amortize such assets over their estimated useful lives.

In December 2008, the FASB issued FSP No. FAS 140-4 and FIN 46(R)-8, Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities (FSP FAS 140-4 and FIN 46(R)-8). FSP FAS 140-4 and FIN 46(R)-8 changes the accounting and reporting for transfers and securitizations of financial assets and the use of qualified special purpose entities (QSPEs) and other variable interest entities (VIEs) by modifying the rules for de-recognition of transferred financial assets, eliminating the concept QSPEs and modifying the consolidation model for VIEs to require a continual reassessment of consolidation conclusions. The consolidation model will include a two-step approach that will consider qualitative attributes of the relationship with a VIE as well as a quantitative approach that analyzes the expected losses and expected residual returns of the VIE. FSP FAS 140-4 and FIN 46(R)-8 is effective for the Company as of December 31, 2008. The Company currently does not securitize any of its financial assets through QSPEs and its relationship with VIEs has not been material.

3. BUSINESS ACQUISITIONS

2007 Acquisitions

Acquisition of HemoCue

On January 31, 2007, the Company completed its acquisition of POCT Holding AB (HemoCue), a Sweden-based company specializing in point-of-care testing, in an all-cash transaction valued at approximately $450 million, including $113 million of assumed debt. HemoCue is the leading international provider in point-of-care for hemoglobin, with a growing share in professional glucose and microalbumin testing.

In conjunction with the acquisition of HemoCue, the Company repaid approximately $113 million of debt, representing substantially all of HemoCue s existing outstanding debt as of January 31, 2007.

The Company financed the aggregate purchase price of $344 million, which includes transaction costs of approximately $7 million, of which $2 million was paid in 2006, and the repayment of substantially all of HemoCue s outstanding debt with the proceeds from a $450 million term loan and cash on-hand. On May 31, 2007, the Company refinanced this term loan. In January 2008, the Company received a payment of approximately $23 million from an escrow fund established at the time of the acquisition which reduced the aggregate purchase price to $321 million.

The acquisition of HemoCue was accounted for under the purchase method of accounting. As such, the cost to acquire HemoCue was allocated to the respective assets and liabilities acquired based on their estimated fair values as of the closing date. The consolidated financial statements include the results of operations of HemoCue subsequent to the closing of the acquisition.

Of the aggregate purchase price of $321 million, $298 million was allocated to goodwill, $38 million was allocated to customer relationships that are being amortized over 20 years and $39 million was allocated to technology that is being amortized over 14 years.

In addition to the amortizable intangibles noted above, $53.8 million was allocated to tradenames, which is not subject to amortization, and $4.0 million was allocated to in-process research and development (IPR&D). The IPR&D was expensed in the Company s results of operations during the first quarter of 2007, in accordance with FASB Interpretation No. 4, Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method, and is included in other operating (income) expense, net within the consolidated statements of operations.

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Supplemental pro forma combined financial information has not been presented as the acquisition is not material to the Company s consolidated results of operations.

Acquisition of AmeriPath

On May 31, 2007, the Company completed its acquisition of AmeriPath, in an all-cash transaction valued at approximately $2.0 billion, including approximately $780 million of assumed debt and related accrued interest. AmeriPath is a leading provider of anatomic pathology, including dermatopathology, and esoteric testing and generated annual revenues of approximately $800 million.

Through the acquisition, the Company acquired all of AmeriPath s operations. AmeriPath, with its team of approximately 400 board certified pathologists, operates 40 outpatient anatomic pathology testing locations and provides inpatient anatomic pathology and medical director services for approximately 200 hospitals throughout the United States. The Company financed the all-cash purchase price and related transaction costs, together with the repayment of approximately $780 million of principal and related accrued interest representing substantially all of AmeriPath s debt, as well as the refinancing of the term loan used to finance the acquisition of HemoCue, with $1.6 billion of borrowings under a five-year term loan facility, $780 million of borrowings under a one-year bridge loan, and cash on-hand. In June 2007, the Company completed an $800 million senior notes offering. The net proceeds of the senior notes offering were used to repay the $780 million bridge loan. See Note 9 for further descriptions of the Company s debt outstanding.

The acquisition of AmeriPath was accounted for under the purchase method of accounting. As such, the cost to acquire AmeriPath was allocated to the respective assets and liabilities acquired based on their estimated fair values as of the closing date. The consolidated financial statements include the results of operations of AmeriPath subsequent to the closing of the acquisition.

The following table summarizes the Company s purchase price allocation of the cost to acquire AmeriPath:

	Estimated Fair Values as of May 31, 2007
Current assets	$ 200,930
Property and equipment	125,817
Intangible assets	561,300
Goodwill	1,415,193
Other assets	67,685
Total assets acquired	2,370,925
Current liabilities	141,435
Long-term liabilities	213,044
Long-term debt	801,424
Total liabilities assumed	1,155,903
Net assets acquired	$ 1,215,022

The acquired amortizable intangibles are being amortized over their estimated useful lives as follows:

	Estimated Fair Value	Weighted Average Useful Life

Customer relationships	$ 327,500	20 years
Non-compete agreement	5,800	5 years
Tradename	2,500	2 years

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In addition to the amortizable intangibles noted above, $226 million was allocated to certain tradenames, which are not subject to amortization.

Of the amount allocated to goodwill and intangible assets, approximately $100 million is expected to be deductible for tax purposes.

During 2008, the Company decreased the amount of goodwill recorded in connection with the acquisition of AmeriPath by approximately $45 million, primarily as a result of changes in judgments regarding the realization of certain pre-acquisition net operating loss carryforwards.

2006 Acquisitions

Acquisition of Focus Diagnostics

On July 3, 2006, the Company completed its acquisition of Focus Technologies Holding Company (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 develops and markets diagnostic products. It offers its reference testing services and diagnostic products to large academic medical centers, hospitals and commercial laboratories. The Company financed the aggregate purchase price of $205 million, which included $0.5 million of related transaction costs, and the repayment of substantially all of Focus Diagnostics outstanding debt with $135 million of borrowings under its secured receivables credit facility and with cash on-hand.

The acquisition of Focus Diagnostics was accounted for under the purchase method of accounting. As such, the cost to acquire Focus Diagnostics was allocated to the respective assets and liabilities acquired based on their estimated fair values as of the closing date. The consolidated financial statements include the results of operations of Focus Diagnostics subsequent to the closing of the acquisition.

Of the aggregate purchase price of $205 million, $142 million was allocated to goodwill, $33 million was allocated to customer relationships that are being amortized over 10-15 years and $9.1 million was allocated to trade names that are not subject to amortization. Substantially all of the goodwill is not expected to be deductible for tax purposes.

Supplemental pro forma combined financial information has not been presented as the acquisition is not material to the Company s consolidated financial statements.

Acquisition of Enterix

On August 31, 2006, the Company completed its acquisition of Enterix Inc. (Enterix), a privately held Australia-based company that develops and manufactures the InSure Fecal Immunochemical Test, a Food and Drug Administration (FDA)-cleared test for use in screening for colorectal cancer and other sources of lower gastrointestinal bleeding, for approximately $44 million in cash. The acquisition is not material to the Company s consolidated financial statements.

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Pro Forma Combined Financial Information

The following unaudited pro forma combined financial information for the years ended December 31, 2007 and 2006 assumes that the AmeriPath acquisition and related financing, including the Company s June 2007 senior notes offering, were completed on January 1, 2006. Supplemental pro forma combined financial information for HemoCue, Focus and Enterix has not been presented as the acquisitions are not material to the Company s consolidated results of operations (in thousands, except per share data).

	2007	2006
Net revenues	$ 7,038,781	$ 7,020,980
Net income	263,225	593,677
Basic earnings per common share:		
Net income	$ 1.36	$ 3.01
Weighted average common shares outstanding basic	193,241	196,985
Diluted earnings per common share:		
Net income	$ 1.35	$ 2.98
Weighted average common shares outstanding diluted	195,262	199,542

The unaudited pro forma combined financial information presented above reflects certain reclassifications to the historical financial statements of AmeriPath to conform the acquired company s accounting policies and classification of certain costs and expenses to that of Quest Diagnostics. These adjustments had no impact on pro forma net income. Pro forma results for the year ended December 31, 2007 exclude transaction related costs of $44 million, which were incurred and expensed by AmeriPath in conjunction with its acquisition by Quest Diagnostics.

4. TAXES ON INCOME

The Company s pretax income (loss) from continuing operations consisted of $1.02 billion, $920 million and $1.02 billion from U.S. operations and approximately $(1.2) million, $(7.1) million and $8.6 million from foreign operations for the years ended December 31, 2008, 2007 and 2006, respectively.

The components of income tax expense (benefit) for 2008, 2007 and 2006 were as follows:

	2008	2007	2006
Current:			
Federal	$ 299,937	$ 267,138	$ 360,806
State and local	57,750	59,625	93,292
Foreign	3,833	1,093	4,586
Deferred:			
Federal	20,764	23,787	(26,897)
State and local	10,029	10,774	(24,206)
Foreign	(5,545)	(3,843)	
Total	$ 386,768	$ 358,574	$ 407,581

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A reconciliation of the federal statutory rate to the Company s effective tax rate for 2008, 2007 and 2006 was as follows:

	2008	2007	2006
Tax provision at statutory rate	35.0%	35.0%	35.0%
State and local income taxes, net of federal benefit	4.6	4.6	4.3
Impact of foreign operations	(1.1)	(0.8)	0.3
Non-deductible expenses, primarily meals and entertainment expenses	0.5	0.3	0.3
Other, net	(1.0)	0.2	(0.5)
Effective tax rate	38.0%	39.3%	39.4%

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets (liabilities) at December 31, 2008 and 2007 were as follows:

	2008	2007
Current deferred tax assets:		
Accounts receivable reserves	$ 82,594	$ 54,226
Liabilities not currently deductible	135,825	95,615
Total current deferred tax assets	$ 218,419	$ 149,841
Non-current deferred tax assets (liabilities):		
Liabilities not currently deductible	$ 125,693	$ 117,647
Stock-based compensation	55,413	36,664
Net operating loss carryforwards	52,394	29,131
Depreciation and amortization	(423,074)	(393,134)
Total non-current deferred tax liabilities	$ (189,574)	$ (209,692)

During 2008, the Company increased deferred tax assets related to accounts receivable reserves by approximately $32 million, with a corresponding decrease in goodwill, for changes in estimates regarding the realization of tax benefits associated with acquired reserve balances.

At December 31, 2008 and 2007, non-current deferred tax liabilities of $190 million and $210 million, respectively, are included in other long-term liabilities in the consolidated balance sheet.

As of December 31, 2008, the Company had estimated net operating loss carryforwards for federal, state and foreign income tax purposes of $73 million, $647 million and $42 million, respectively, which expire at various dates through 2028. As of December 31, 2008 and 2007, deferred tax assets associated with net operating loss carryforwards of $66 million and $71 million, respectively, have each been reduced by a valuation allowance of $14 million and $42 million, respectively.

Income taxes payable including those classified in other long-term liabilities in the consolidated balance sheets at December 31, 2008 and 2007, were $88 million and $83 million, respectively.

As of January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements and provides guidance on the recognition and measurement of tax positions taken or expected to be taken by an entity. The adoption of FIN 48 resulted in an increase to our contingent tax liability reserves of $30 million with corresponding charges to retained earnings, goodwill and additional paid-in capital. The contingent liabilities for tax positions under FIN 48 primarily relate to uncertainties associated with the realization of tax benefits derived from certain state net operating loss carryforwards, the allocation of income and expense among state jurisdictions, the characterization and timing of certain tax

deductions associated with business combinations and employee compensation, and income and expenses associated with certain intercompany licensing arrangements.

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The recognition and measurement of certain tax benefits includes estimates and judgment by management and inherently involves subjectivity. Changes in estimates may create volatility in the Company s effective tax rate in future periods and may be due to settlements with various tax authorities (either favorable or unfavorable), the expiration of the statute of limitations on some tax positions and obtaining new information about particular tax positions that may cause management to change its estimates.

The total amount of unrecognized tax benefits as of and for the years ended December 31, 2008 and 2007 consists of the following:

	2008	2007
Balance, beginning of year	$ 107,943	$ 91,856
Additions:		
for tax positions of current year	3,775	14,341
for tax positions of prior years	3,916	14,698
Reductions:		
Changes in judgment	(32,684)	(1,494)
Expirations of statutes of limitations	(2,724)	(4,423)
Settlements	(9,349)	(7,035)
Balance, end of year	$ 70,877	$ 107,943

The total amount of unrecognized tax benefits as of December 31, 2008, that, if recognized, would affect the effective tax rate is $51 million. Based upon the expiration of statutes of limitations, settlements and/or the conclusion of tax examinations, the Company believes it is reasonably possible that the total amount of unrecognized tax benefits for the items previously discussed may decrease by up to $34 million within the next twelve months.

Accruals for interest expense on contingent tax liabilities are classified in income tax expense in the consolidated statements of operations. Accruals for penalties have historically been immaterial. As a result of changes in judgment and favorable resolutions of uncertain tax positions, $5 million of net interest was credited to income tax expense in 2008. Interest expense included in income tax expense in 2007 was approximately $6 million. As of December 31, 2008 and 2007, the Company has approximately $18 million and $23 million, respectively, accrued, net of the benefit of a federal and state deduction, for the payment of interest on uncertain tax positions. The Company does not consider this interest part of its fixed charges.

In the regular course of business, various federal, state and local and foreign tax authorities conduct examinations of the Company s income tax filings and the Company generally remains subject to examination until the statute of limitations expires for the respective jurisdiction. The Internal Revenue Service has completed its examinations of the Company s consolidated federal income tax returns up through and including the 2004 tax year. The Company is currently appealing an issue with regards to its 2005 tax year. Certain state tax authorities are conducting audits for various years between 2004 and 2007. In December 2008, the Company reached a settlement agreement to pay a state tax authority approximately $44 million in taxes, penalties and interest ($26 million, net of federal and state benefits) for certain tax positions associated with intercompany licensing arrangements. This settlement is expected to be paid in 2009. At this time, the Company does not believe that there will be any material additional payments beyond its recorded contingent liability reserves that may be required as a result of these tax audits. As of December 31, 2008, a summary of the tax years that remain subject to examination for the Company s major jurisdictions are:

United States	federal	2004	2008
United States	various states	2004	2008

In conjunction with its acquisition of SmithKline Beecham Clinical Laboratories, Inc. (SBCL), which operated the clinical testing business of SmithKline Beecham plc (SmithKline Beecham), the Company entered into a tax indemnification arrangement with SmithKline Beecham that provides the parties with certain rights of indemnification against each other.

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5. SUPPLEMENTAL CASH FLOW AND OTHER DATA

	2008	2007	2006
Depreciation expense	$ 227,300	$ 209,975	$ 184,844
Interest expense	(185,476)	(186,329)	(96,454)
Interest income	5,712	8,015	5,029
Interest, net	(179,764)	(178,314)	(91,425)
Interest paid	189,294	157,502	102,055
Income taxes paid	359,336	315,745	381,348
Businesses acquired:			
Fair value of assets acquired	$	$ 2,954,728	$ 278,078
Fair value of liabilities assumed		1,395,867	28,453

6. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at December 31, 2008 and 2007 consisted of the following:

	2008	2007
Land	$ 35,786	$ 36,272
Buildings and improvements	365,481	360,442
Laboratory equipment, furniture and fixtures	1,182,376	1,042,890
Leasehold improvements	348,821	318,552
Computer software developed or obtained for internal use	259,851	255,408
Construction-in-progress	57,478	92,918
	2,249,793	2,106,482
Less: accumulated depreciation and amortization	(1,370,106)	(1,194,484)
Total	$ 879,687	$ 911,998

7. GOODWILL AND INTANGIBLE ASSETS

The changes in goodwill, net for the years ended December 31, 2008 and 2007 are as follows:

	2008	2007
Balance as of January 1	$ 5,220,104	$ 3,391,046
Goodwill acquired during the year	9,260	1,799,101

Other purchase accounting adjustments	(120,105)	5,955
(Decrease) increase related to foreign currency translation	(54,333)	24,002
Balance as of December 31	$ 5,054,926	$ 5,220,104

For the year ended December 31, 2008, goodwill acquired during the year was associated with several immaterial acquisitions. Other purchase accounting adjustments were primarily due to changes in estimates regarding the realization of certain pre-acquisition net operating loss carryforwards, the reduction in certain acquired pre-acquisition tax loss contingencies, and a payment received from an escrow fund established at the time of the

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HemoCue acquisition (see Note 3 for further discussion). Approximately 90% of the Company s goodwill as of December 31, 2008 and December 31, 2007 was associated with its clinical testing business.

For the year ended December 31, 2007, goodwill acquired during the year was primarily related to the acquisitions of AmeriPath and HemoCue, and other purchase accounting adjustments were primarily due to the impact on goodwill as a result of the adoption of FIN 48. (See Notes 3 and 4 for further discussions).

Intangible assets at December 31, 2008 and 2007 consisted of the following:

	Weighted Average Amortization Period	December 31, 2008			December 31, 2007		
		Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Amortizing intangible assets:							
Customer-related intangibles	19 years	$ 585,963	$ (99,384)	$ 486,579	$ 589,418	$ (70,036)	$ 519,382
Non-compete agreements	5 years	54,382	(48,298)	6,084	53,832	(46,476)	7,356
Other	13 years	53,934	(13,258)	40,676	64,214	(8,394)	55,820
Total	19 years	694,279	(160,940)	533,339	707,464	(124,906)	582,558
Intangible assets not subject to amortization:							
Tradenames		294,064		294,064	304,175		304,175
Total intangible assets		$ 988,343	$ (160,940)	$ 827,403	$ 1,011,639	$ (124,906)	$ 886,733

Amortization expense related to intangible assets was $37.3 million, $27.9 million and $10.8 million for the years ended December 31, 2008, 2007 and 2006, respectively.

The estimated amortization expense related to amortizable intangible assets for each of the five succeeding fiscal years and thereafter as of December 31, 2008 is as follows:

Fiscal Year Ending December 31,	
2009	$ 36,086
2010	35,309
2011	35,049
2012	33,831
2013	32,851
Thereafter	360,213
Total	$ 533,339

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8. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses at December 31, 2008 and 2007 consisted of the following:

	2008	2007
Trade accounts payable	$ 191,219	$ 205,067
Accrued wages and benefits	299,374	318,285
Accrued expenses	412,106	359,355
Accrued settlement reserves	316,920	242,009
Total	$ 1,219,619	$ 1,124,716

9. DEBT

Short-term borrowings and current portion of long-term debt at December 31, 2008 and 2007 consisted of the following:

	2008	2007
Borrowings under Secured Receivables Credit Facility	$	